

SOME ECONOMIC AND LEGAL ASPECTS OF REAL ESTATE

WITH PARTICULAR REFERENCE TO SOUTH AFRICA

by

PETER PENNY

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<u>Chapter</u>		<u>Page</u>
	PREFACE	
I	INTRODUCTION	1
II	THE VALUATION OF REAL ESTATE	6
	A General Principles	6
	1. Market Value	6
	2. The Valuation Process	7
	3. The Methods of Valuation	8
	(a) Direct Comparison	8
	(b) Indirect Comparison	9
	(c) Replacement Cost Approach	10
	4. Value to the Owner	11
	B Aspects of the Method of Indirect Comparison	12
	1. The Capitalisation Rate and Depreciation	12
	2. Valuation where Income declines or is of Limited Duration	16
	(a) The Inwood Formula	18
	(b) The Hoskold Formula	19
	(c) The Straight Line Method	20
	(d) The Equal Decline Annuity Method	21
	(e) The Compound Rate Decline Annuity Method	22
	(f) The Methods Compared	23
	3. The Reversion	24
	4. Yield	25
	(a) Comparison of Investment Media	25
	(b) The "Build-up" and "Band of Investment" Methods of Finding the Capitalisation Rate	27
	(c) The Influence of the Tenant upon the Appropriate Yield	28
	5. Estimation of Replacement Cost	29
	6. Development Project Valuation	31
	(a) Formula to Establish the Value of a Development Site	32
	(b) Formula to Establish the Optimum Development of a Site	33

<u>Chapter</u>		<u>Page</u>
III	TOWN PLANNING, URBAN RENEWAL AND ECONOMICS	35
	The Role of Economics in Planning	35
	The Justification for Planning	36
	The Objectives of Planning	39
	Planning and Land Values	40
	Steps in Planning	43
	Town Planning in South Africa	45
	The Nature of Urban Renewal	50
	The Necessity for Urban Renewal	54
	The Scale of Urban Renewal	55
	The Execution of Urban Renewal	55
	The Criticisms of Urban Renewal	57
	Urban Renewal in South Africa	62
	Cost-Benefit Analysis	63
IV	COMPENSATION UPON EXPROPRIATION	68
	Introduction	68
	The Administrative and the Judicial Decree Methods	69
	Market Value or Value to the User?	70
	Severance Damage	77
	Consequential Damage	80
	When must the Whole be taken?	80
	Temporary or Intrinsic Value?	82
	Admissible Evidence	83
	What Interests must be Compensated?	86
	Four Important Enactments	88
	(a) The Railway Expropriation Act	88
	(b) The Expropriation Act	89
	(c) The Cape Municipal Ordinance	89
	(d) The Community Development Act	93
V	THE COMPENSATION AND BETTERMENT PROBLEM IN TOWN PLANNING	100
	Part 1 - General Considerations	100
	The Meaning of Betterment	101
	Recoupment	101

ChapterPage

Set-off	102
Direct Charges	102
The 1947 Act	104
Floating and Shifting Value	105
The Difficulty of Collecting Betterment	106
The Payment of Compensation	108
The Economic Incidence of Betterment	111
Betterment and the Cost of Accommodation	111
Who Pays the Public's Piper?	112
An Attempt to State a General Principle	112
Part 2 - An Examination of the Situation in the Four Provinces of South Africa	118
(a) Compensation	118
(b) Betterment	120
APPENDIX A - The Land Commission Act 1967 in Britain	124
VI RATES	127
Part 1 - General Considerations	127
Introduction	127
Rating and the Criteria of Sound Taxation	127
(a) Ability to bear	128
(b) Benefits received	128
(c) Reliability	130
(d) Economical administration	130
(e) Minimum distortion	131
(f) Social expediency	131
Site Value Rating	131
Potential Value v. Rebus Sic Stantibus	136
The Incidence of Rates	138
What Value?	140
Flat, Composite, Site and Differential Rating	141
Equity and Rating as between Different Types of Property	142
Conclusion	143

<u>Chapter</u>		<u>Page</u>
	Part 2 - The South African Position	145
	The Cape Valuation Ordinance	147
VII	THE VALUATION OF LAND FOR SUBDIVISION	151
	Part 1 - The Economic Principles	151
	Part 2 - The South African Case Law	156
	The Braamfontein Case	156
	The Geldenhuys and Kleinfontein Cases	159
	The Glencairn Buildings Case	159
	The Coronation Case	163
	The Cape and Transvaal Case	164
	The Randfontein Case	166
	S.A. Railways v. New Silverton	168
	Krause v. S.A.R. & H.	169
	The Florida Hills Case	169
	The Steelpark Case	173
	The Risi Investments Case	175
	The Arbitration Proceedings between City Deep Limited and Johannesburg City Council	175
	Conclusion	177
	APPENDIX A - Formulae for Valuing Land with Township Potential	178
VIII	RENT CONTROL	181
	Introduction	181
	The Case for Rent Control	182
	The Criticisms of Rent Control	184
	Injustice to Owners of Controlled Property	185
	Deterioration of Property	186
	Decrease in Rented Accommodation	188
	Control Deters Development	189
	Arbitrary Redirection of Expenditure to Other Sectors of the Economy	190
	Disrupts Allocation of Space	191
	Determination of Rent	191
	A Note on Building Control	197

<u>Chapter</u>		<u>Page</u>
IX	CONCLUSION	199
	A Trained Profession	199
	A Specialist Tribunal	202
	The Allocation of Land Resources: The Market or the State?	204
	APPENDIX A - Recapitulation	207

PREFACE

Earlier drafts of all except the first and last chapters of this thesis have been published as articles, both in the hope that conclusions reached would have some practical influence and in the fear that pressure of business commitments might prevent the completion of the work as a whole. A further reason for publication of these papers was to expose ideas formulated to the test of criticism; in the process I have benefitted from the helpful comment of so many that it would be invidious to attempt to single out those to whom my indebtedness is greatest. There are, however, three persons of whom I am bound to make mention: Mr Z.S. Gurzynski, Professor E.W.N. Mallows and Mrs June Stevenson.

As my supervisor, Mr Gurzynski has been a stimulating mentor, ever generous of his time; Professor Mallows has provided me with an insight into the processes and philosophies of planning which otherwise I would have lacked; my colleague and one-time secretary, Mrs Stevenson, has been my constant task-master, setting aright both the illogic of my reasoning and the inelegance of my language. Without her, this thesis might not have been written.

It remains to acknowledge the places of publication of papers (1) which have formed drafts of this work:

Chapter 2	South African Chartered Accountant, August 1968.
Chapter 3	South African Journal of Economics, June 1968.

.....

(1) These papers were in each case discussed with Mr Gurzynski as being an integral part of this thesis and his approval of publication was obtained.

Chapter 4	South African Law Journal, May 1966.
Chapter 5	South African Journal of Economics, December 1966.
Chapter 6	South African Journal of Economics, June 1967.
Chapter 7	South African Law Journal (to be published in May and August 1969).
Chapter 8	South African Law Journal, November 1966.

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CHAPTER I

INTRODUCTION

The essential purpose of this study is to assess the effect of action by the State, both legislative and judicial, on the value and utilisation of land and buildings; it does not set out to provide a general statement on the principles of land economics (1). The boundaries of the subject matter have been established by problems arising in the professional practice of a property economist in South Africa, rather than on any a priori basis. The title, "Economic and Legal Aspects of Real Estate with particular reference to South Africa", may imply a broader examination than has in fact been made. At the outset therefore it must be stated that there are other matters which might well have been embraced by such a title, but which were not objectives of this study - for example the policy of successive governments towards the utilisation of land by Non-Whites.

The study commences in Chapter II with a statement on valuation procedures because these are basic to the understanding of subsequent material and because they are little understood in South Africa by legislative bodies, by the judiciary, and indeed by those whose livelihood is earned in the real estate field. The meaning of the term "market value" is considered in this chapter and the broad principles of the valuation process are discussed. Thereafter more detailed attention is given to valuation by the method of Indirect

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- (1) To the writer's mind the best analysis of these principles is to be found in Turvey, "The Economics of Real Property", published by George Allen & Unwin Ltd., London. Other works of consequence are referred to at appropriate places in the course of the present study.

Comparison which is the normal method for valuing commercial, industrial and investment property. The reader with a sound knowledge of valuation principles may find a study of this chapter unnecessary, but an acquaintance with these principles is essential for an understanding of the fourth and subsequent chapters. This chapter does not attempt a complete description of valuation techniques (2); its essential purpose is to furnish a set of tools to be applied in assessing the subject matter discussed in the latter part of the study.

The third chapter is intended to provide a general statement on the impact of the State on land usage through town planning and urban renewal. It begins by showing the relationship of economics to town planning and proceeds to a consideration of the objectives and steps in planning. Planning legislation in South Africa is outlined. The nature, necessity, scale and execution of urban renewal are then considered. The criticisms levelled against urban renewal and the form that urban renewal takes in South Africa are discussed. Finally the chapter considers the validity and importance of cost-benefit analysis in town planning.

Chapters IV and V examine two important consequences of State action on real estate: firstly the question of compensation where expropriation takes place, and secondly the problem of compensation or betterment where there is no expropriation but where the value of real estate is affected by State action. The fourth chapter commences by stating the principle which it is thought should underlie expropriation and then proceeds to an assessment of the extent to which this principle is observed. The relative merits of the administrative

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- (2) For a more complete treatment of real estate valuation see Lawrance, Rees and Britton "Modern Methods of Valuation" 5th edition, published by the Estates Gazette, London, and "The Appraisal of Real Estate", 3rd edition, published by the American Institute of Real Estate Appraisers, Chicago.

and the judicial decree approaches to expropriation are considered and the problem of whether compensation should be at market value or value to the user is discussed. More detailed problems commented upon are severance and consequential damage, and the questions of when the whole property should be taken, whether the value to be found is temporary or intrinsic, what evidence is admissible and what interests must be compensated. Finally, certain important South African enactments are examined.

The subject matter of the fifth chapter, as has been indicated, is complementary to that of the fourth in that it deals with the question of compensation and betterment where land is not actually expropriated but where its value is affected through State action. It is divided into two parts, the first devoted to general considerations and the second to the situation in the four provinces of South Africa. The chapter begins by outlining the meaning of the terms "betterment", "recoupment", "set-off" and "direct charges". The concepts contained within and the consequences arising from the Uthwatt Committee's report and the 1947 Town and Country Planning Act in Britain are then examined, and comment is made on the difficulty of collecting betterment, on its economic incidence, and on its effect upon the cost of accommodation. The circumstances in which compensation is paid are discussed and an attempt is made to state a general principle as a solution to the problem of compensation and betterment. In part 2 the law relating to compensation and betterment in South Africa is outlined, and the peculiarly South African concept of endowment is examined. The chapter ends with an appendix on the Land Commission Act, 1967, in Britain.

The next chapter, the sixth, is again divided into two parts, the first being related to general considerations, and the second to the South African position. It is concerned principally with the equity of rating as a form of taxation and the methods of application of rating which will result in the least inequity and create the minimum of economic distortion. Rating as a form of taxation in the light

of the criteria of a sound tax is examined. The controversial subject of site rating is discussed, and more detailed matters considered are whether rates should be based upon potential value or value in existing use, where the economic burden of rates falls, whether rates should be assessed on "value to the owner", "market value" or some arbitrary formula, and the question of the equity of rating as between different types of property. The second part of the chapter describes the broad system of rating in the four provinces of South Africa and ends with a more detailed discussion of the controversial Cape Valuation Ordinance.

In the seventh chapter the procedure for valuing land with township potential is explained and there is a discussion of the approach which has been taken by South African courts to this problem. Part 1 of the chapter deals with the economic principles and part 2 contains a seriatim examination of the South African cases.

Rent control, which is the subject of the eighth chapter, represents action on the part of the State which has material social consequences. The chapter considers these consequences and then turns to the question of the amount at which the controlled rent is fixed in South Africa. A note on the like problem of building control is appended.

In Chapters III to VIII suggestions are made, where it is thought possible and necessary, for more reasonable ways of approaching solutions to problems raised; the ninth and final chapter supplements these by stating certain conclusions which are not dealt with therein and which it is believed would bring about a better approach to land valuation and utilization. The appendix to this chapter is a recapitulation of proposals for reform arising from the previous chapters thus identifying and highlighting the conclusions reached in the study.

Something requires to be said of the constitutional structure of South Africa although an examination of political matters is no part of the purpose of this study. The Act of Union of 1910 passed by the Parliament in Westminster gave to South Africa a constitution

which was neither truly unitary nor truly federal. Although the Act established provincial governments it left it open to the central legislature of the Union to impose its will upon the Provincial Councils and indeed, if it so wished, to abolish the semi-federal system which came into existence. Because of this semi-federal constitution there is a far greater body of legislation relating to property than would exist in a country with a unitary constitution. Not only has the central government passed legislation on town planning, expropriation and the like, but the four Provincial Councils too have exercised their rights to legislate on such matters. The principles upon which enactments dealing with similar problems are based often differ and sometimes the powers of the central government and the provincial governments overlap so that there is uncertainty as to how problems arising in land usage are to be resolved.

The economy of South Africa has less emphasis on private enterprise than that of the United States, but generally more than that of Britain, although in some of its aspects, particularly those which deal with such matters as the control of African labour, the power of the State is greater than in Britain. In legislation affecting property there has been a slow movement to the economic left. It is suggested that this is not because socialist philosophies predominate in South Africa, but because the implications of legislation have not always been understood and models from elsewhere (particularly from Britain) have been followed without their consequences being appreciated. Where legislation has borne harshly upon the private citizen it is the writer's opinion that this has stemmed not so much from deliberate disregard for the property owner's welfare as from ignorance of the consequences of State action.

It is the writer's hope that this study will serve to clarify the objectives of State action in the field of land usage, to draw attention to deleterious consequences of present legislation and judicial interpretation and to restate the functions of the market in the allocation of land resources.

CHAPTER II

THE VALUATION OF REAL ESTATE

A GENERAL PRINCIPLES

1. MARKET VALUE (1)

The word 'value' has been burdened with a multitude of epithets. Although these have often been empty verbiage, it is a fact that the 'value' estimate for a property will vary according to the purpose of the valuation. Thus a property may well have more than one 'value' at any one time, depending on the particular objective in view, e.g. take-over bid, expropriation, sale, rates assessment, death duties.

The 'market' or 'exchange' value of a thing is determined by its utility, its scarcity and the competitive wants of purchasers. It represents the point of equilibrium between supply and demand at any one moment. In real estate valuation, the 'thing' to be valued is the group of rights attaching to a property. Because the term 'property' is commonly used as a convenient ellipsis for this group of rights, it should not be thought that it is the property as such which is being valued. Both State activity, such as town planning, and action on the part of private citizens, such as the grant of leases or servitudes, can materially affect value and must be carefully weighed in the valuation process. Market value is an estimate of the price that will be obtained for a property

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(1) See discussion of the concept in Chapter IV at page 70 and in Chapter VII at page 176.

where a sale is assumed in circumstances in which all buyers and all sellers:

- (i) have reasonable knowledge of the purposes for which properties available in the market are capable of being used and the future income or amenities which they are likely to produce;
- (ii) take reasonable steps to compare properties with available substitutes;
- (iii) act intelligently and without compulsion.

It should be noted that in practice the real estate market is imperfect and both buyers and sellers are likely to be incompletely informed. Nevertheless market value is based upon the prediction of the future benefits that will accrue from a property and is established by the price at which substitute interests can be bought.

2. THE VALUATION PROCESS

Valuation is not a mystique; its methods are essentially scientific although the data available are typically imprecise, necessitating subjective assessment. The accuracy of valuation depends upon the degree of comparability of the evidence obtainable. Properties can be compared directly by reference to selling prices or indirectly on the basis of potential income which can be capitalised into value. In the absence of evidence of comparable sales or comparable rents the appraiser may be forced to resort to the technique of estimating replacement cost and deducting depreciation. Such a valuation will inevitably be unscientific because, as will be shown below, there is no satisfactory way of estimating depreciation without reference to sale prices or rents. Substitution is the basic principle of valuation. The decisions of both buyers and sellers as to price will be derived from the cost at which an equivalent property could be bought, hired or built. The buyer will take account of all three possibilities and will not pay more for the property to be valued than the figure at which he could acquire a reasonable

substitute (2). The demand for any property is said to be elastic when a rise or fall in the price causes a significant fall or rise in demand. Demand is inelastic when a rise or fall in price causes relatively little fall or rise in demand. The existence of good substitutes for a property tend to make the demand for that property elastic. The less adequate are substitutes and the more inelastic is demand, the more arbitrary is any estimate of value.

Frequently the appraiser's forecasts and calculations will be of more use to the client than the estimate of value derived from them. It is therefore important that they should be included in the valuation report and that the degree of uncertainty thought to attach to any prediction should be stated. The practice still prevalent in South Africa of presenting a client with an unexplained conclusion is to be condemned. Nor is any authority lent to such an unsubstantiated figure by cloaking it in the garb of a sworn appraisement.

3. THE METHODS OF VALUATION

A 'valuation' is an estimate of 'value'. Three approaches to making the value estimate must be considered.

(a) Direct Comparison

In terms of this method properties are valued by direct comparison of selling prices. This method is useful in the valuation of undeveloped sites and of houses. In respect of other types of property it is unlikely to be appropriate except where buildings are of similar construction, and even in this case there will probably be too many variables for

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- (2) When no reasonable substitute is available the buyer will not pay more than the value in use which the property will have for him. See discussion below under heading "Value to Owner".

direct comparison to be practicable.

(b) Indirect Comparison

The indirect or capitalisation method (3) enables property to be compared on a basis of quality and quantity. Two steps have to be taken: first, the earning potential of the space must be estimated by comparison with other property; secondly, the capitalisation factor must be determined by considering the opportunity cost of the purchase price, that is, the rate of return obtainable by the investor on alternative investments with comparable characteristics.

For this method to be applicable there must be evidence of comparable rents. It is not necessary that the property should actually be let, for where it is occupied by its owner the rent can be taken to be that at which it could be let. The method involves consideration of both the market for the hire of property and the market for the purchase of property. It is the normal method of valuing commercial, industrial and investment property.

The 'Profits' method of valuation is a variation of the method of indirect comparison which will have to be employed when the annual value of space used for commercial or industrial purposes cannot be assessed by comparison with the rent at which other space is let (i.e. when there is not sufficient evidence of the rent at which reasonably equivalent space can be hired). Turnover is estimated and deductions are made therefrom to allow for working expenses and a fair return on working capital, having regard to the risks of the business. The residual figure is the amount which the occupant could reasonably be expected to pay as rent.

.....

(3) Sometimes described as the investment method.

This figure is capitalised in order to find the capital value of the premises (4).

(c) Replacement Cost Approach

This procedure is known in Britain as the 'contractor's method' and in the United States as the 'summation method'. The site and building are valued separately, their sum being taken to be the value of the property as a whole. The value of the building is found by estimating its present replacement cost and deducting an amount for depreciation (5). The method is not regarded with favour by property economists. The value of a property is no more the sum of the value of the site and the replacement cost of the building than the value of a motor-car is the sum of the cost of replacing its various parts. Moreover, when the design of a building is such that a similar structure would not again be built, there is little justification for contemplating what would be the present cost of its erection. In the case of a new building that is a sensible improvement of the site it is quite probable that cost and value will coincide, but this is highly unlikely where an old structure is to be valued. Costs affect value only in so far as they influence the supply of space coming on to the market. The method is in fact only appropriate in the case of property with special characteristics making comparison with other properties impracticable. Through lack of evidence of sales or rents it may have to be used, for example, in the case of factories which are so specialised as to be unadaptable for general use.

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- (4) In consequence of the nature of the assumptions upon which it is based, the profits method of valuation is highly imprecise and should only be used in the absence of any alternative method of valuation and then with considerable caution.
- (5) For comment on the concept of depreciation refer Chapter VI page 149.

There is in fact no logical manner in which depreciation can be estimated other than by reference to market value. As a measure of last resort the summation method must occasionally be used. It is of the utmost importance that the appraiser should state why he has not been able to use some other procedure and should warn the recipient of his report that the estimate of value therein is inevitably arbitrary to a degree. It should be noted, however, that the replacement cost of a property will always establish a ceiling to its value.

4. VALUE TO THE OWNER (6)

The value to the owner (or user) has sometimes to be estimated. It may, for example, be required for balance sheet purposes, where a business is to be sold as a going concern, or where a property to be expropriated has a value to the owner in excess of its market value.

For the owner, the value of a property is equivalent to the sum of the direct and indirect loss that he would incur if the property were taken from him. The lower limit of value is established by market value because this has been defined in terms of the price at which the owner could expect to sell the property. It is clear that the value to the owner cannot be less than the sum which he could obtain on sale. Similarly, the upper limit of value is established by what the owner would have to pay in order to acquire a reasonably equivalent property (including such costs as would be consequent upon moving). Nothing can be worth more than the cost of a satisfactory substitute. Thus the upper limit is set by the lesser of:

- (i) the price at which an owner of a substitute developed property would be prepared to sell and
- (ii) the price at which the owner of a substitute undeveloped property would be prepared to sell plus the cost of rebuilding

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(6) See discussion of this concept in Chapter IV at page 70.

less such depreciation as can be attributed to physical deterioration and functional obsolescence (7).

The actual level of the value to the owner will be established by the profits method of valuation which has been described above, provided that it will not be less than the lower limit established by market value or more than the upper limit set by the cost of replacement (if such be possible).

When the figure produced by the profits method is lower than market value no problem arises, but when the profits method gives a higher figure than replacement cost (in circumstances where replacement is possible) the difference between replacement cost and the figure shown by the profits method is attributable to goodwill. If a property can be replaced with one which is its complete equivalent (or better) there will be no loss of goodwill. To the extent that perfect substitution is not possible, the substitute property will have less value to the owner than the taken property and the difference will be part of the value to the owner of the taken property. It should be observed that with special purpose industrial property the value to the owner will frequently be in excess of market value.

B ASPECTS OF THE METHOD OF
 INDIRECT COMPARISON

1. THE CAPITALISATION RATE AND DEPRECIATION

It has been noted above that the normal method of valuing commercial, industrial or investment property is the method of indirect comparison, otherwise described as the investment or capitalisation method. The capitalisation rate is the factor by which all the future benefits arising from a property should be discounted in order to produce the

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(7) If depreciation has to be estimated, all the difficulties which have been outlined will inevitably be encountered.

price (8). Whilst discounted cash flow techniques appear to be something of an innovation in the assessment of business enterprises they have been employed as basic tools for several decades by property economists, as indeed by actuaries. Nevertheless, the problems of capitalisation and depreciation remain amongst the most controversial in valuation theory.

Several theoretical solutions to the problem of translating income into value have been propounded which are dependent upon estimating the remaining useful life of a building and, in some cases, dependent upon knowing the appropriate yield on the site alone and the appropriate yield on the building alone (9). In actual experience virtually no evidence exists upon which these three factors can be estimated. Actuarial life expectancy tables for investment buildings cannot be compiled. There can never be any reasonable degree of certainty about the time that a building will remain an economic improvement of the site because this will depend overwhelmingly upon environmental factors and not to a significant extent upon its physical condition.

In the writer's view the capitalisation rate (i.e. the yield) reflects the risk of variation in income or capital value in the future and specific allowance for depreciation is necessary only in exceptional cases. Where the risk of future reduction in income is high, the capitalisation rate will be high. Depreciation as such is unpredictable and it is the fear of a decline in income which leads a purchaser to use a higher capitalisation rate

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(8) For a general introduction to compound interest calculations see: Maisel, 'Financing Real Estate', page 147 et seq., Merret & Sykes, 'The Finance and Analysis of Capital Projects' chapter I; Lawrance, Rees & Britton, 'Modern Methods of Valuation', 5th edition, page 461 et seq. or Hutchinson, 'Commercial Arithmetic', 8th edition, page 260 et seq.

(9) See, for example, Babcock 'Real Estate Valuation', and 'Ellwood, Tables for Real Estate Appraising and Financing'.

although in the assessment of leasehold (10) investments sinking fund calculations may have to be made.

A further objection to methods of valuation which make specific allowance for depreciation is that they assume that the market value of a property is at its peak at the time of appraisal and that there will be no fluctuation in market value despite any changes that may take place in demand. It is apparent that such assumptions are not realistic and that a property may well appreciate with the passage of time.

In order to allow for taxation a factor (11) must be applied to both the net income flow and the capitalisation rate. Where income assumed to endure for perpetuity is capitalised, allowance for taxation is immaterial because the same factor is applied to both the numerator and the denominator of the equation (12), but where deferment or other compound interest calculations (13) are made the

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- (10) A leasehold is an investment in which the rent paid by the tenant is less than the rent at which the tenant is able to sublet. The difference between the rent paid by the tenant and the rent which is or can be obtained from a sub-tenant is known as the "profit rent" and the right to its receipt for the duration of the lease has a capital value. With the effluxion of time the holder of a long lease at a fixed rent will frequently find that the rent he has contracted to pay has become less than the market rent.
- (11) $1 - t$ where t is the amount of tax in the pound expressed as a decimal fraction. The amount t where market value is to be assessed is the rate of taxation thought to be typical in the market and not the rate payable by a purchaser. The writer has usually found it satisfactory to regard the current rate of company tax as the typical rate. The decision of the individual investor as to whether to purchase or sell will, however, be based upon the rate of tax that he himself must pay, so that the value of a property to an individual may differ from its market value.
- (12) For equation where income is assumed to endure for perpetuity see Example 1 below.
- (13) For equations where income declines or is of limited duration see Examples 2 - 6 below.

taxation factor does not cancel out and allowance for taxation is essential. Further, in the case of sinking fund calculations, allowance must be made not only for the effect of taxation on the rate of compound interest, but also for its effect on annual instalments because these are not allowable deductions for tax purposes.

The approach which, in the writer's opinion, ought to be employed in the absence of special circumstances is based upon an estimate of income for the first few years less an allowance for foreseeable annual expenditure. It is assumed that this net income will endure for perpetuity because this is considered to be the least arbitrary assumption, specific allowance is not made for depreciation, and the capitalisation rate is employed to allow for the hazard of change.

Capital value can be derived from net income by multiplying the figure of net income by a factor. This factor is known as the "Year's Purchase" (YP) figure.

When income is in perpetuity, the YP can be found very simply by dividing 100 by the required rate of return, expressed as a percentage, i.e. the Year's Purchase is the reciprocal of the capitalisation rate expressed as a decimal function. The formula is therefore as follows:

$$YP = \frac{1}{i}$$

where i is the required rate of return expressed as a decimal function.

Example 1:

Assume:

	Net Income	R10,000	
	Capitalisation rate	8%	
Then	Capital value	= R10,000	$\times \frac{1}{0.08}$
		= R125,000.	

2. VALUATION WHERE INCOME DECLINES OR
IS OF LIMITED DURATION

Two situations require to be considered:

- (i) where income will remain constant during a period and terminate at the end of the period;
- (ii) where income will decline over a period.

Where allowance is made for amortization, the method chosen is dependent upon the assumptions made about the future behaviour of the annual and capital value of the property. Where it is assumed that the income will be constant and will then stop abruptly, sinking fund calculations can be made on the basis of either of two assumptions. Firstly, that the sinking fund concept is only hypothetical and reinvestment will take place at a rate equal to the risk or capitalisation rate (sometimes known as the Inwood Formula or Single Rate Method). Secondly, that a sinking fund to accumulate at a rate below the capitalisation rate of interest will actually be set up with a financial institution (sometimes called the Hoskold Formula or Double Rate Method). The second assumption is unlikely to be appropriate for freehold calculations and would also not generally be used in leasehold calculations. What sense is there in investing at, say, $3\frac{1}{2}\%$ when, with not unreasonable risk, a much higher yield

can be obtained elsewhere? Moreover, if inflation occurs it will severely affect the real sum accumulated in the sinking fund by the end of the period. It should be noted that YP in the Inwood formula represents two possible ways of regarding the problem. Firstly, it represents the present value of a series of payments receivable over a period; secondly, it is also equivalent to the capital sum upon which an annual income of R1 will provide both simple annual interest at i and annual instalments for a sinking fund which will compound at i per annum to YP at the end of n years. It is preferable to regard the formula from the first point of view because in circumstances where the Inwood formula is thought appropriate it is improbable that a sinking fund would actually be set up. It should also be noted that if the risk rate and the sinking fund accumulation rate are taken to be equal, the Hoskold formula will produce an identical result to that which would be achieved by employment of the Inwood formula. Other approaches to amortization are the Straight Line Method which assumes that in each year of the period of the investment an equal capital sum will be returned to the investor so that by the end of the investment's life the investor will have recaptured his entire capital, the Equal Decline Annuity Method, which is based on the assumption that income will decrease by an equal amount in each year, and the Compound Rate Decline Annuity Method, which assumes that income will decline at a compound rate per cent per annum.

The declining annuity formulae may in particular circumstances represent a reasonable approach to valuation, but there is little to commend the straight line method because no investment could behave in accordance with its assumptions and a more realistic conclusion would be reached by the employment of whichever other approach was thought most appropriate in the light of the assumed behaviour of the investment.

The valuations achieved by the different methods show a considerable variation, as illustrated by the following examples:

(a) The Inwood Formula (14)

Example 2 (Taxation disregarded)

Assume:

Net Income R10,000

Capitalisation rate 8%

Life of investment 50 years

$$\begin{aligned}
 \text{Then Capital Value} &= \text{R10,000} \times \frac{1 - \frac{1}{(1 + 0.08)^{50}}}{0.08} \\
 &= \text{R10,000} \times 12.233 \quad (15) \\
 &= \text{R122,330.}
 \end{aligned}$$

.....
 (14) The Inwood Formula is:

$$\text{YP} = \frac{1 - \frac{1}{(1 + i)^n}}{i}$$

where i = required rate of return expressed as a decimal function.
 and n = period of receipt of the annuity.

(15) This factor can be found in Parry's Valuation Tables, 8th Edition at page 30.

(b) The Hoskold Formula (16)

Example 3 (Taxation disregarded)

Assume:

Net Income R10,000

Capitalisation rate 8%

Sinking Fund
Accumulation rate 3%

Life of Investment 50 years

Then Capital value = $R10,000 \times \frac{1}{0.08 + \frac{0.03}{(1 + 0.03)^{50} - 1}}$

= R10,000 x 11.253 (17)

= R112,530.

.....

(16) The Hoskold Formula is:

$$YP = \frac{1}{i + Z}$$

where i = Required rate of return expressed as a decimal function.

where Z = Annual sinking fund instalment which will accumulate to R1 at the end of n years.

$$= \frac{X}{(1 + X)^n - 1}$$

n = Period of receipt of the annuity.

and X = Interest per annum on R1 invested in sinking fund expressed as a decimal function.

(17) This factor can be found in Parry's Valuation Tables, 8th Edition at page 16.

(c) The Straight Line Method (18)

Example 4 (Taxation disregarded)

Assume:

Net income in first R10,000
year

Capitalisation rate 8%

Life of investment 50 years, i.e. recapture of 2%
of capital value p.a.

Then Capital Value = R10,000 x $\frac{1}{0.08 + 0.02}$

= R100,000.

.....

(18) The straight line method formula is:

$$YP = \frac{1}{i + d}$$

where i = the required rate of return expressed as a decimal function.

and d = the rate of recapture of principal expressed as a decimal function.

(d) The Equal Decline Annuity Method (19)

Example 5 (Taxation disregarded)

Assume:

Net income in first
year R10,000
Capitalisation rate 8%
Life of investment 50 years
Annual decrease in
income R200

$$\text{Then Capital value} = R10,000 \times A - 200 \times \frac{A - 50 \times V^{50}}{0.08}$$

$$\text{Where } V = \frac{1}{(1 + 0.08)}$$

$$\text{And } A = \frac{1 - V^{50}}{0.08}$$

$$= R94,000.$$

.....
(19) The equal decline annuity method formula is:

$$YP = A - Q \times \frac{A - n \times V^n}{i}$$

where i = the required rate of return expressed as a decimal function.

n = the period of receipt of the annuity.

Q = the amount by which the annuity decreases per annum over n years.

$$V = \frac{1}{(1 + i)}$$

$$\text{and } A = \frac{1 - V^n}{i}$$

(e) The Compound Rate Decline Annuity Method (20)

Example 6 (Taxation disregarded)

Assume:

Net income in first
year R10,000

Capitalisation rate 8%

Life of investment 50 years

Annual decrease in
income 3% compound

Then Capital Value = R10,000 x $\frac{1 - V^{50}}{i}$

$$\text{Where } V = \frac{1}{1 + i}$$

$$i = (1 + x)(1 + y) - 1$$

$$x = 0.08$$

$$y = 0.03$$

$$= R80,000.$$

.....
(20) The compound rate decline annuity formula is:

$$YP = \frac{1 - V^n}{i}$$

$$\text{Where } i = (1 + x)(1 + y) - 1$$

x = required rate of return expressed
as a decimal function.

y = annual compound rate of decline in
income expressed as a decimal function.

$$V = \frac{1}{1 + i}$$

n = period of receipt of the annuity.

(f) The Methods Compared

Several matters requiring comment arise from Examples 1-6 above. The answers to Examples 1 and 2 do not differ materially; it can be seen that the income receivable after 50 years is of little consequence and it is in fact accepted valuation practice to treat any flow of income assumed to continue in constant amount for 50 years as lasting for perpetuity. The procedure used in Example 3 results in a significant fall in value. However, the assumption of capital recapture (Example 4) or decline in income (Examples 5 and 6) has a much more drastic effect on present value. The writer's preference, as has been previously stated, is generally to use the simple procedure illustrated in Example 1. It is worth noting that answers identical to those in Examples 2, 3, 4, 5 and 6 would be produced if, in Example 1, the rate applied to the net income was increased, respectively, to 8.2%, 8.9%, 10%, 11.7% and 12.5%.

With regard to the use of these methods in practice, in his professional experience the writer has most commonly used the formula of $YP = \frac{1}{i}$ and has also employed the Inwood formula and the Compound Rate Decline Annuity formula with some frequency but has never found occasion to resort to the Hoskold formula, the Straight Line formula or the Equal Decline Annuity method. The use of the Inwood formula has been necessary where income is of a limited duration and the Compound Rate Decline Annuity formula where the real level of income under a lease has been affected by inflation.

It should be noted that where it is expected that income will rise by an equal amount in each year YP can be found by altering the minus sign in front of the letter Q in the formula in the footnote 19 to a plus sign, and that where an annual compound rate of increase is expected YP can be found by altering the plus sign in front of the

letter y to a minus sign in the formula in footnote 20 (21).

3. THE REVERSION

In circumstances where a property is subject to a lease the method of capitalising income assumed to endure for perpetuity is unlikely to be appropriate and it will usually be necessary to treat the income during the lease and the reversion separately, the reversion being the capital value which a property will possess on the termination of a lease. The rent arising under the lease will be discounted as an income flow for a limited period of time. The present value of the reversion at any time during the currency of a lease can be found by multiplying the amount of the reversion by the factor for the present value of R1.00 receivable at a given date in the future (22). When the lease is of long duration the capital value of the reversion is conjectural. Although buildings become obsolete, a change in the cost structure of the building industry, such as a real increase in African wages, can cause existing buildings to appreciate; although the demand for land relative to its supply tends to increase, this will not necessarily be so in the case of any individual property; a change in the general level of interest rates may raise or lower the value of all investment property. Moreover, it is probable that political and social developments will invalidate

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(21) Thus the Equal Income Increase Annuity formula would be:

$$YP = A + Q \times \frac{A - n \times V^n}{i}$$

and the Compound Rate Increase Annuity formula would be:

$$\frac{1 - V^n}{i}$$

$$\text{where } i = \frac{(1 + x)}{(1 + y)} - 1$$

$$(22) \frac{1}{(1 + i)^n}$$

where "i" is the interest on R1 per annum expressed as a decimal function and "n" is the period of years remaining before the expiry of the lease.

any prophecy of value projected more than a relatively few years into the future. The valuer may find some consolation in the fact that the compound interest element inherent in the process of deferment will mean that even a considerable error of judgment as to the ultimate capital value of the reversion will probably not greatly affect the result if the lease is of any length. The rise of the rent to its true level at the end of a lease will cause capital appreciation which (at least in South Africa) will not be taxable. For this reason the prices paid for reversions are likely to exceed the figures of value calculated by applying the present value of R1 formula to the capital value of the property at the end of the lease. What any individual ought to pay for a prospective tax free gain can only be calculated in the light of the rate of tax payable by that individual.

4. YIELD

(a) Comparison of Investment Media

The market for investments can be regarded as a whole and property can be compared with other securities competing for the funds of investors. The most important determinant of yield is the opportunity cost of capital, i.e. the rate obtainable on an alternative investment of equal risk and magnitude. The value of any investment is found by discounting the anticipated net income at a rate of interest equal to the yield obtainable on alternative investments with similar characteristics. Consequently yield reflects the attraction of alternative investment opportunities. Comparisons can thus be made between the rates of return in the property market and in those other markets which compete for the funds of lenders and investors. The return on gilt edged securities and on shares, and the rate of interest charged on loans, throw light on the appropriate yield rates for use in property valuation. Provided other factors do not intervene to affect one particular class of property investment more than others, the relationship

between the yield from various properties will be maintained when there is a general rise or fall in interest rates.

Because stock exchange and property investments are broad substitutes, the yields on these two types of investment tend to move together over a period. A rise in stock exchange prices will lower the yield at which property investments can be sold. It should be noted that in the case of shares it is common to quote the dividend yield after company tax has been paid; on the other hand, property yields are commonly based on the net rent without any regard being had to the tax which the recipient must pay. It frequently happens that companies retain profits to be used for future growth and the yields on the dividends reflect the growth possibilities. This would make for a lower yield on shares, other things being equal. As has already been indicated, property is essentially a long-term investment and yields in the property market only follow fluctuations in the stock market when it becomes evident that these will persist over a period. Property yields are also related to those on long-term government stock. Although there tends always to be a time lag between a movement in the price of government stock and in the property market, the former is convenient for comparison with the latter. It should be noted that there has to be a tangible movement over a few months before the effect is perceptible in the rates on property and that government stock yields may also be misleading because they may be deliberately maintained at artificial levels by State action for reasons of policy.

The rate of interest at which mortgage finance can be obtained has a particularly important effect on real estate yields. A fall in mortgage interest rates, *ceteris paribus*, will raise the prices at which properties can be sold. The basis on which mortgage money can be obtained is a better guide than the yield on debentures because evidence of the appropriate yield should always be sought as close as possible to the market for the commodity to be valued. The best evidence of the yield to be employed in valuing a particular

property is the yields at which comparable properties have been purchased. Yields within the property market will vary widely depending upon the difficulty in managing the particular investment, its liquidity, its size and, above all, the risk thought to attach to it. Even properties of the same type differ markedly in the degree of security they provide.

(b) The "Build-up" and "Band of Investment"
Methods of Finding the Capitalisation Rate

Use is made in the United States of what are known as "build-up" capitalisation rates. The assumption is made that capitalisation rates consist of pure interest (time preference), that is the rate of interest obtainable on long-term government securities, plus an allowance for risk, plus an allowance for management, plus an allowance for lack of liquidity.

The writer does not believe that a capitalisation rate can be built up by identifying and adding the factors for which it admittedly makes allowance. The market does not provide evidence by which these components of the capitalisation rate can be quantified. However, the build-up rate concept is useful in so far as it serves to emphasise the factors of which a capitalisation rate must take account. Moreover, once the general capitalisation rate for a particular type of property has been found by comparison with the returns on other types of investment and from the evidence of previous sales, the concept behind the "build-up" method does provide a useful aid for adjusting the capitalisation rate of different properties of the same type.

Another approach to finding the capitalisation rate is known as the "band of investment" method (23). This method assumes that it will be known what rate of interest will be charged on mortgage loans,

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(23) See Ellwood loc. cit.

the percentage of the market value of the property which will be advanced as a loan and the return which investors are demanding on the equity percentage in property investment. The writer has not found this method satisfactory because the terms of mortgage loans vary so considerably and there is little evidence available of the return which investors obtain on equity, i.e. on the actual capital invested in property. Whatever theoretical arguments there may be in favour of such an approach, it is not practicable because the evidence needed for its application is simply not available.

(c) The Influence of the Tenant Upon
the Appropriate Yield

The considerations that may affect the rate of interest can be divided between those relating to the property and those relating to the tenant. The build-up method of capitalisation which, as discussed above, attempts to produce the capitalisation rate by a process of addition, emphasises that the factors which affect the rate for a property relate to management, liquidity and the risk of change in net income. The contract with the tenant has significance for all three.

With regard to management it is better from an investment point of view to have less income with complete freedom from responsibility for repairs and maintenance. Where the property is occupied by a single strong tenant the management element is small. Liquidity is also often enhanced by a lease to a strong tenant because a property occupied under a long lease to a strong concern will generally be more saleable than one without such a lease. The risk element is reduced because the rent of a strong concern will be paid with greater certainty and promptitude. The tenancy of a large multiple concern gives exceptional security to the income because a multiple company is not dependent upon the trade of a

particular locality. The net lease (24) has the advantage of being free from outgoings of uncertain amount; a long lease spares the landlord from voids and the possibly considerable expense of adapting the premises for a different trade. Where the rent under the contract is below the vacant market rental it may be regarded as very well secured and may reasonably be capitalised at a lower rate per cent than would be appropriate in dealing with the full annual value of the premises. Where the contract rent exceeds the market rent, its continued receipt rests upon the financial standing of the tenant. This requires an increase in the yield rate.

5. ESTIMATION OF REPLACEMENT COST

The problem sometimes arises that the replacement cost of a property has to be estimated, for example on expropriation. The method of estimating replacement cost of a developed property as at the date of expropriation is set out below. It is to be noted that this procedure would only be appropriate where a building was new and represented a sensible improvement of a site so that it could reasonably be thought that replacement cost and value were equal.

Let

x	=	site cost
A	=	first instalment of building cost
B, C, D, etc	=	subsequent instalments of building cost
n	=	period from date of site acquisition to completion of building
a	=	period from first instalment of building cost to completion of building
b, c, d, etc	=	period from subsequent instalment of building cost to completion of building
i	=	interest rate expressed as a decimal function

.....

(24) A lease in terms of which all running expenses are paid by the tenant.

Note

- (1) The formula for the present value of R1 receivable at the end of n years is:

$$\frac{1}{(1+i)^n}$$

- (2) The formula for the present value of R1 per annum receivable for a period of n years is:

$$\frac{1}{i} \left[1 - \frac{1}{(1+i)^n} \right]$$

Then

Replacement cost as at date of expropriation is:

$$\begin{aligned} & x + xi \times \frac{1}{i} \left[1 - \frac{1}{(1+i)^n} \right] + A \times \frac{1}{(1+i)^{n-a}} \\ & + Ai \times \frac{1}{i} \left[1 - \frac{1}{(1+i)^a} \right] \times \frac{1}{(1+i)^{n-a}} \\ & + B \times \frac{1}{(1+i)^{n-b}} \\ & + Bi \times \frac{1}{i} \left[1 - \frac{1}{(1+i)^b} \right] \times \frac{1}{(1+i)^{n-b}} \\ & + C \times \frac{1}{(1+i)^{n-c}} \\ & + Ci \times \frac{1}{i} \left[1 - \frac{1}{(1+i)^c} \right] \times \frac{1}{(1+i)^{n-c}} \\ & \text{etc.} \end{aligned}$$

6. DEVELOPMENT PROJECT VALUATION (25)

In any assessment of a development scheme, allowance has to be made for the fact that a fully let building does not appear overnight. The project has to be considered at a point in time - usually the date of the purchase of the site. Both the cost of construction and the commencement of rent will not occur until well after the site has been bought. The value that the building will have on completion of letting must be estimated by applying a capitalisation rate to the net income, and a deferment factor must then be applied to the capitalised rent in order to find its present value as at the date of the purchase of the site. Similarly, a deferment factor must be applied to building cost in order to find its present value at the time that the site is bought. Usually it is sufficiently accurate to take one date during the construction period (being the approximate midpoint in the occurrence of cost) as if it were the date on which the total building cost was incurred.

Deferment of capitalised rent and of building cost allows for interest during the construction period. It should be noted that interest lost on the developer's own capital is no less important than interest he must pay on borrowed funds because through investing his money in a property he is sacrificing the opportunity of obtaining a return on an investment elsewhere. The rate of interest appropriate for deferment is the developer's opportunity cost, i.e. the rate he could obtain on an alternative investment of equal magnitude and risk. This can be taken to be the same as the rate used to capitalise net income in order to estimate the value of a property on completion. Thus a single rate of interest ought to be used throughout the calculation, that is for both capitalisation and deferment.

In valuing a development scheme it should be noted that the yield must provide a margin for the greater risks involved in purchasing

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(25) For discussion of land for township development see Chapter VII.

and developing a site as compared with purchasing an existing building. The inclusion of a capital sum labelled "Developer's Profit" merely confuses the calculation and is not a sound practice. Annual yield is a simple, accepted and understood tool in the assessment of competing investment alternatives, and its use is less arbitrary than the addition of "Developer's Profit" to capital cost.

Formula to Establish Value of a Development Site

A procedure known as the "Residual Method" is employed in order to establish the value of vacant land for investment purposes. The formula used to find the price which ought to be paid for a development site is:

Formula (a)

Site Value = Capitalised Rent deferred -
Building Cost deferred.

Let

Site Value = S
Required rate of return per annum on R1 = i (expressed as a decimal function)
Net Rent = R (assumed to endure for perpetuity)
Building cost = B
Period of deferment of capitalised rent = P
Period of deferment of building cost = Q

Then

Formula (b)

$$S = \frac{R}{i} \times V^P - B \times V^Q$$

Where $V^n = \frac{1}{(1 + i)^n}$ = the present value of a receipt (or an expenditure) of one rand deferred for "n" years.

It should be noted that it is normal practice to assume that the same rate of interest should be used for capitalisation of rent, deferment of capitalised rent and deferment of building cost.

Formula to Establish Optimum

Development of a Site

The problem envisaged is where site cost is known and the costs of, and rents produced by, various design alternatives can be estimated. The optimum alternative will be that which shows the highest yield on capital outlay (that is the highest figure for "i").

The figure "i" will be the only unknown in formula (b) and by solving for "i" in the case of each of the design alternatives the scheme which shows the highest yield can be found.

However, a precise solution for "i" is not mathematically possible and approximations have to be used. The following first approximation (26) has been devised:

Formula (c)

$$i = \frac{R + (Z)^2 \times B \times Q}{B + R \times P \times S}$$

when Z is an approximation to "i" obtained by

$$i = \frac{R}{S + B}$$

From tests formula (c) has been found to be insufficiently accurate and the following second and more accurate approximation has been developed:

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(26) In the development of formulae (c) and (d) the writer is indebted to an actuarial friend, Mr Erin Fitchett, for supplementing the deficiencies in his mathematics.

Formula (d)

$$i = \frac{R}{B + R \times P + S - KL}$$

Where K = "i" in formula (c)

$$\text{and } L = \frac{R \times P(P - 1)}{2} + BQ$$

Alternatively, the approximate yield can be established by trial and error through the use of Present Value tables (27). The table most closely approximating the actual rate of interest is that which most nearly provides the same figure for site value as for capitalised rent deferred less building cost deferred (see formula (a) above).

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(27) i.e. Tables showing the present value at varying interest rates of a unit of currency receivable at the end of a period, e.g. Parry's Valuation Tables, 8th Edition, pp. 51 et seq.

CHAPTER III

TOWN PLANNING, URBAN RENEWAL AND ECONOMICS

THE ROLE OF ECONOMICS IN PLANNING

It is not uncommonly the case that town planners who have had no training in economics regard the subject with suspicion if not hostility. They see it as a device employed by the holders of purse-strings to baulk planning proposals. This is a grave and dangerous misconception for economics is not only a helpful tool for the planner, but an integral and utterly vital part of the planning process. The discipline of economics is concerned with the allocation of resources which are in limited supply. It has to do with the fact that rational action in the pursuit of any objective can be achieved only when there is full realisation of the sacrifice of other objectives that will be involved. It strives to provide a basis for so allocating resources to any one objective that no greater benefit would be derived from devoting these resources elsewhere. It is a method of analysis which demonstrates that in the pursuit of any objective a point is reached at which further or marginal increments in resources could more beneficially be devoted to other objectives (1). The function of the economist is to identify the costs and benefits which will flow from any planning proposal in order that resources may be rationally allocated. His role in planning has been likened to that of the consultant to a business

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(1) See Hutt, "Economic Aspects of Town Planning", a paper presented to the Institute of Municipal Treasurers and Accountants of South Africa, in 1958, page 144.

organisation whose task is firstly to clarify the goals of the organisation, and secondly to find the most efficient (least-cost) means of achieving these goals (2).

THE JUSTIFICATION FOR PLANNING

The city serves both social and economic purposes. It has been described as being both an amenity and an apparatus of production (3). As an economic mechanism it evolved to facilitate the production, distribution and consumption of goods and services. In the absence of planning, the allocation of land resources within the city was a function of the demand for and the supply of sites. Although land allocation in the past was lacking in central direction, it was not haphazard. The price mechanism operated through the unrelated but overwhelmingly rational decisions of innumerable people to produce an urban form which was essentially functional. Nevertheless, because the real estate market is imperfectly competitive, because social values at times conflict with the dictates of the price mechanism and because the advance in technology necessitates a highly complex infrastructure that only a public authority can provide, it has become almost universally accepted that town planning represents a justifiable interference with the free working of the economy. The pattern of land use which would be brought about by competition provides a guide to the preferences of the community which for all its inadequacy remains the best available to us because what consumers will pay is the only objective test of consumers' satisfaction.

Ratcliff has asserted (a) that the principal purpose of planning should be to produce that pattern of land use which would be created by a perfectly competitive market, (b) that the fundamental need for planning arises simply because the actual conditions of the market do

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(2) Davis and Whinston, "The Economics of Urban Renewal", reprinted in "Urban Renewal: The Record and the Controversy", edited by Wilson page 51.

(3) See Hutt, op. cit. page 141.

not accord with the hypothesis of perfect competition, and (c) that the vital function of the city planner is therefore to mitigate market imperfections in order to enhance the efficiency of land use (4). In the view of the writer, Ratcliff places insufficient emphasis on the increasing technology of modern society and the growing scale of infrastructure that the public authority must provide if productivity is to be maintained within the private sector (5). The question of the optimum nature of this infrastructure is at least as fundamental as any other facing planners. Further, the private process of land utilisation may be inadequate because, inter alia, units of ownership are frequently too small for economic redevelopment, individual owners often have insufficient means for redevelopment or are unaware of the potentials of redevelopment, many different stages in economic life may be represented in a neighbourhood, and, above all, because monopolistic positions frequently exist (6).

It has been argued that if we had had planning in the past we would now have better housing, that towns would have been developed in a manner more suited to modern conditions and that the environment would be more aesthetically pleasing. These assertions are debatable; certain functions, such as roads, have in fact been subject to central direction to a greater or lesser extent because for some commodities and services markets did not easily arise, and if planning had been more general it is questionable whether the forecasts of the planner about future requirements of society would in fact have provided for these any better than did the free operation of the market. The pattern of land usage in any society will be a function of the scarce resources available to that society at any time. Because nineteenth century industrial housing in Britain does not conform with twentieth

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 (4) See generally Ratcliff, "Urban Land Economics", page 385.

(5) It is not disputed that the essential purpose of planning is to enhance the operation of the market (see discussion below under the heading "The Objectives of Planning").

(6) See Ratcliff, "Private Investment in Urban Redevelopment", pages 2 and 3.

century standards (7), it does not follow that it represented a less than optimum allocation of resources at the time that it was erected. Nor has planning always produced more aesthetically satisfactory land utilisation than free enterprise. The fundamental case for planning must rest on other grounds. The justification for interference with the market arises where the social cost of devoting a property to a particular use exceeds the private cost or where the social benefit exceeds the private benefit. The case for controlling development arises where the developer either does not bear all the costs of the development or does not receive all the benefit (8). Private costs and benefits, as defined by Pigou (9), are the costs incurred and the benefits received by the person carrying out an undertaking, while the social costs and benefits of an undertaking are those flowing to the community (including the person who carries out the undertaking) (10).

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- (7) See Hutt, op. cit. page 136.
- (8) See Turvey, Journal of the Town Planning Institute, September/October 1955, page 270. Turvey writes, loc. cit.: "Planning is required to do for an area in many separate ownerships what good estate management will do if the whole area has a single owner. The owner of land sufficient for a few houses will not find it worthwhile to set aside a part as open space, since most of the benefits of the open space would accrue to dwellings not in his ownership. But where, as in the case of Bloomsbury, a whole area is in one pair of hands, the use of some building land for open space may be in the owner's interest. He loses the building value of the squares but gains the resulting increase in the value of the rest of the land. Because this other land is also owned by him his private benefit includes all the social benefit and thus his private interest coincides with the social interest, so that interference is not necessary."
- (9) See "Economics of Welfare", Part 2, Ch. 2.
- (10) In "Facts and Fiction in Urban Renewal", a paper published by the Philadelphia Housing Association in "Ends and Means of Urban Renewal" at page 25, Winnick has stated the case for planning in the following words: "The unaided private investor - no matter how enlightened - cannot give us a city in the image we desire. For private redevelopers can seldom assemble sites of optimal size or location. They make do with what they can. Frustrated by multiple titles, by existing leases and stubborn holdouts, by the existing street system and unpurchasable public buildings, they forgo their best opportunities for the next best; they design their structures according to the size and shape of the site they are able to get."

THE OBJECTIVES OF PLANNING

Lichfield has listed the following objectives of land planning:

1. regard for interests of the national and local economy;
2. regard for the objectives of all public authorities;
3. preservation, protection and creation of amenity;
4. protection of assets;
5. resistance to the aggravation of problems of the area;
6. securing co-ordinated development;
7. raising standards of development;
8. keeping available for development, sites which will be required for specific purposes;
9. securing that development is well situated in relation to other existing or proposed development (11).

The first of these objectives is the most important. The principal purpose of city planning has been stated to be that it supports the economic base of a community (12). The second objective is of doubtful validity. The third objective is the most readily understood and the fourth perhaps the most popular. The fifth objective is legitimate but its abuse should be guarded against. For example, it does not necessarily follow that because increased density in the development of a Central Business District will cause traffic congestion, the permissible floor areas of new buildings should be reduced. The sixth and eighth objectives are important and often overlooked by the public as well as by the private sector. The seventh objective is

(11) See "Economics of Planned Development", pages 30 - 34.

(12) See Nelson and Aschman, "Real Estate and City Planning". Pen-nance "Housing, Town Planning and the Land Commission" writes at page 14: "The fundamental case for the planning of land use is now generally expressed in economic terms of improving the market's efficiency in allocating scarce resources so as to maximise economic welfare (however defined)."

patently worthy, and the ninth is similar to the sixth. A further function of regulating the future use of land is to facilitate the operation of the real estate market by creating greater certainty (although planning practice sometimes has the reverse result). It will be apparent that the distinction made on occasion between physical planning and economic planning is artificial and erroneous. In consequence of our inability to foresee the future accurately and of the scarcity of the resources available to us to transform cities substantially, the objectives of planning must necessarily be limited. However, although the planner cannot control the major economic forces which create cities, the changes which he can make to the natural pattern are of no little significance to society (13).

PLANNING AND LAND VALUES

Writers on town planning have at times made statements to the effect that good planning will create the highest possible land values or that successful town planning enhances the total value of property in a town (14). To the extent that town planning can attract new demand to a town by increasing its efficiency or amenity, or can hold demand which in the absence of town planning might move away from a town, such statements have substance. On the other hand it has been held by Ratcliff that the difference in the rent of a

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- (13) See Reynolds, "Economics, Town Planning and Traffic", page 140. To the writer it seems presumptuous to claim, as Hall does, that "the distribution of the different sorts of land uses, and the broad pattern and variation of land values which follow upon that distribution, are the gifts of the planner." See Hall "The Land Value Problem and its Solution" in "Land Values" at page X. A similar view is put forward by Day in "The Case for Betterment Charges" in "Land Values" at page 99.
- (14) Amongst South African writers, see Floyd, "Town Planning in South Africa", page 107, and Kantorowich, "The Problem of Redevelopment of Central Areas in Rapidly Expanding Communities", delivered at a conference of the Commission for Technical Co-operation in Africa South of the Sahara, in January 1959, at page 10.

relatively inaccessible site is the saving in transport costs enjoyed by the occupier of the former, that the object of planning is to minimise the 'costs of friction' (i.e. the sum of site rents and transport costs) and that the optimum town plan (disregarding the possibility that the plan leads to an increase in the total demand for land) is that which produces the lowest aggregate land value within the town (15). Lean and Goodall dispute Ratcliff's assertion and contend that rent is not merely a charge for a saving in transport costs to the user of a site, but a charge based on the utility which he receives from it (16). They hold that from the viewpoint of economics the criterion of a town planning scheme is that it should lead to the highest land values because this signifies the most efficient utilisation of resources.

They write:

"If one person can produce more goods and services in value than another person with the same co-operating resources from a given piece of land, then that person will be willing and able to compete successfully for the land against the other by paying a higher price. Higher land value signifies a better utilisation of that piece of land. With one or two provisos this can be generalised and used with reference to town planning. If town planning leads to higher land values than would exist without it, then a better or more efficient utilisation of resources has been achieved. A corollary of this is that for any given site the best planned town is one where the aggregate land values are at a maximum"(17).

In their opinion a land value criterion will be more objective than one based upon social costs and benefits (18). They state that the only sensible question which an 'economist/town planner' can ask is:

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(15) See Ratcliff, "Urban Land Economics", pages 385, 386. See also Schaaf, "Economic Aspects of Urban Renewal", page 5.

(16) "Aspects of Land Economics", page 246.

(17) Lean and Goodall, op. cit. page 228.

(18) Op. cit. page 237.

"Which town plan will maximise land values?" (19).

A third view is expressed by Reynolds who considers that since land values are merely a reflection of points of attraction, position and transport costs, they can have no independent validity as a planning objective. He writes:

"Planning should merely aim at the optimum layout by comparing the advantages and costs of various developments and the effects on urban land values would be ignored as a planning objective ... since urban land values are merely reflections of other factors there is little merit in making the regulation of them a primary independent objective of town and land-use planning"(20).

It is evident that there is much conflicting and confused thought on the matter of the relationship of town planning and land values. The truth would seem to be that although an increase in accessibility may decrease the difference in value of two sites it does not follow that their aggregate value will fall or that it will rise. Land value is a function of demand and supply and if improved transport has the effect of increasing the supply of land for a particular purpose its average value or price may fall, but from this it cannot be concluded that the aggregate value will increase or decrease. Neither the 'highest land value test' nor the 'lowest land value test' is any test of planning efficiency at all. Both of these alleged criteria take too few of the several complex factors at work into account. There are too many variables affecting land value for it to provide a test of general application of the soundness of planning proposals. However, it is not to be thought that land values are of no relevance to planning: it is probable that much bad planning in the past has

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(19) Op. cit. page 239.

(20) Op. cit. pages 55 and 56. Reynolds, however, furnishes a diagram which shows that if transport costs fall land values will rise (see pages 53 and 55). It is submitted that this diagram is based on a false analysis.

been due to poor understanding by planners of the nature and level of values (21). In the writer's view planning should cause no more change in land values than is the inevitable concomitant of action taken for some other reason.

STEPS IN PLANNING

The basic steps involved in city planning are:

1. Prediction of the pattern that would probably evolve if economic forces were allowed to operate without State interference. In the past it is likely that overwhelmingly the greater part of a city planning scheme would have reflected the natural pattern which would have occurred without it, but with the increasing technology of society the infrastructure provided by the public authority assumes growing importance (22).
2. Decisions as to what modifications of the pattern (i.e. that which would probably have been produced by the price mechanism) are socially or economically desirable (23).
3. Estimates of the practicability of achieving the desired modifications of the natural growth pattern.

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(21) An example of confused thought about planning and land values appears in the report of the Uthwatt Committee. See below Chapter V pages 105-106.

(22) In many situations the product of the myriad single decisions of private enterprise will prove too difficult to predict or will be unpredictable without reference to the infrastructure to be furnished by the public authority; research will have to be employed to uncover the problems which exist and an efficient solution then sought. The writer takes issue with Day's assertions with reference to Britain that "in a free market the pattern of land values would be completely different from what it is today, so there is no justification for regarding the market as the product of laissez-faire market forces". This seems grossly to overestimate the influence of town planning. See Day op. cit. page 100.

(23) It should be noted that the concept of 'economic desirability' embraces 'functional desirability'.

A planning scheme should be adopted only after most diligent research and analysis. Investors act upon the profit motive and if planning adversely affects the potential for profit it will effectively curtail development. The plan ultimately accepted will normally be a compromise between what was desired and what was politically and financially practicable. The financial consequences of any proposal should always be assessed by cost benefit analysis (24). Too frequently town planning schemes have been formulated largely on the judgment of those designing them because the planners concerned were neither acquainted with economics nor in possession of reasonable long-term predictions of demand and population trends.

The unit for city planning should be the metropolitan region and not the area contained within the boundaries of any particular local authority for these are unlikely to form a rational entity for planning purposes (25). Thus the first step in the formulation of a city planning scheme should be the determination of the area which is to be planned. Almost invariably 'dormitory' municipalities will surround the central municipality and will resist incorporation although they will be concerned with the Central Business District as the focus of the metropolitan area. It is essential that the common interests of such communities in town planning should be recognised and that the whole of the metropolitan area be planned as a unit. A metropolitan planning authority at a supra-municipal level ought therefore to be established. As Gulick (26) has stated:

"The underlying problems become impossible of rational attack unless there is a single centre for co-ordinated analysis, planning and action."

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(24) See below under heading "Cost Benefit Analysis".

(25) See Ely and Wehrwein, "Land Economics", page 461; Wendt, "Lessons from the Old World for America's City Builders", Appraisal Journal, July 1961, page 394.

(26) Quoted by Wendt, op. cit. page 394. See also Nelson and Aschman op. cit. pages 150 and 490.

TOWN PLANNING IN SOUTH AFRICA

Modern town planning in South Africa dates from the early 1930's. As a consequence of the semi-federal system of government in the Republic town planning legislation has been passed by both Parliament and the four provincial councils with some resulting overlap and confusion. The authority of the provinces to make laws relating to town planning stems not from the South Africa Act of 1910 (which was the constitution of the Union), but from the Financial Relations Act No. 10 of 1913 as amended by Act No. 46 of 1925 (27). The central government has delegated powers to the four provinces to frame ordinances to control the development of townships (that is, subdivisions of rural land) and to prepare town planning schemes for existing towns.

The Cape Province was the first to make use of the powers given by Act 46 of 1925 in passing Ordinance 13 of 1927, but this was ineffective and it is the Transvaal Ordinance No. 11 of 1931 which has been the model for planning legislation in South Africa. The Cape passed Ordinance 33 of 1934 and Natal passed Ordinance No. 10 in the same year; the Natal ordinance was later replaced by Ordinance No. 27 of 1949. It was not until 1947 that the Orange Free State passed Ordinance No. 20 - prior to this date only township layout had been controlled in the Orange Free State.

The aim of town planning schemes as set out in section 32 of Transvaal Ordinance No. 11 of 1931 was as follows (28): "Every town planning scheme shall have for its general purpose a co-ordinated and harmonious development of the municipality to which it relates

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- (27) See Pretoria City Council v. Levinson 1949(3) S.A.305(AD), and also see Bouchier: "Comments on the Difference in the Town Planning Laws of the Provinces", Proceedings of the Summer School of the South African Institute of Town Planners, pages 20 and 22.
- (28) These words are now substantially embodied in Section 17 of Ordinance 25 of 1965(T) which has repealed the whole of Ordinance No. 11 of 1931(T).

in such a way as will effectively tend to promote health, safety, order, amenity, convenience and general welfare, as well as efficiency and economy in the process of such development".

Similar sections appear in the Cape and Natal ordinances, but although the Free State ordinance is based upon the Transvaal ordinance the O.F.S. Provincial Council omitted to state what aim it had in mind for Town Planning schemes. There is some divergence of view as to whether town planning concepts in South Africa have been adopted principally from the United States or from Britain. Floyd (29) states that words similar to those used in the Cape, Transvaal and Natal ordinances may be found in zoning acts in some states in the United States of America. At the time of the framing of the Transvaal ordinance there was as yet no experience of the zoning of built up areas in England but such experience already existed in the United States. Certainly the principle of clear and specific zoning which exists in South Africa is much more similar to general United States practice than it is to the procedure now used in England in terms of which planning permission has always to be sought. However, it is the view of Bouchier and Kantorowich that South Africa has drawn principally on Britain for a basis for its town planning legislation (30).

The objectives of town planning as stated in the Transvaal, Cape and Natal ordinances accord with the principles set out above under the headings "The Justification for Planning" and "The Objectives of Planning". It should be noted that it is apparent from the Afrikaans text of the Transvaal ordinance which uses the word "besuïning" (31) that the word "economy" in the English text means

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(29) "More about Town Planning in South Africa", page 25.

(30) See Kantorowich, Journal of the Town Planning Institute, September, October 1964 at page 347; and Bouchier op. cit. at pages 20 and 29.

(31) In Ordinance 25 of 1965(T) the word "spaarsaamheid" has replaced the word "besuïning" but this does not appear to alter the intended meaning.

"saving" rather than "maximising productivity". However, the terms "efficiency" and "economy" taken together make it clear that town planning schemes are to have regard to the first of the objectives listed above under the heading "The Objectives of Planning".

Despite the inroad into the planning field of the Central Government through legislation passed by Parliament, the main planning work is still left to the initiative of local authorities in the case of town planning schemes and to private investors and local authorities in the case of townships. The principal control of planning is exercised by the Townships Boards of which there is one in each province. These are the focal points of planning control and act in an advisory capacity to the Provincial Administrators. The main functions of the Townships Boards are to control the schemes and to act as arbiters between objectors to a scheme and local authorities and also to decide appeals against decisions of local authorities (32). Thus the intention of the ordinances is to give the local authorities the initiative and not to make the Townships Boards planning authorities as such (33).

The promulgation of the provincial ordinances established two principles: firstly, that the subdivision of land could only proceed with the approval of a public authority and that this approval would be subject to conditions which would include setting aside land without compensation for public purposes such as roads, open spaces, public utilities, and schools. In the writer's opinion this is a perfectly satisfactory principle to the extent that the

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(32) See Floyd, "Town Planning in South Africa", page 45.

(33) Floyd loc. cit. comments that the intention of the ordinances has been destroyed in the Cape by an amendment passed in 1953, namely section 35 bis, which has deprived the local authority of much of its initiative and given the Provincial Administration the power to alter schemes drastically at any moment. See Floyd, page 106. For a defence of section 35 bis, see Bouchier op. cit. page 22.

owner should be responsible for the cost of proper services (34). Secondly, the ordinances established the principle that from the date that the local authority acclaimed its intention of proposing a scheme all changes in the use of land were entirely at its discretion and no compensation was payable for any planning restriction imposed unless this required the change of an existing usage to one of lower value. Whilst in the writer's opinion this principle was inequitable to owners whose land had a potential for higher usage at the time of the local authority's announcement of its intention to prepare a scheme, in practice as we have earlier observed in this chapter it is unlikely that a significant amount of land would have been zoned for a purpose other than that of its highest potential usage (35).

Besides Municipalities and Provincial Administrations, an abundance of other authorities has been empowered by legislation to deal with matters which have a bearing upon town planning. Divisional councils in the Cape and Peri-Urban Health Boards in the three other provinces control the subdivision of rural land. The Land Survey Act No. 9 of 1927 gives the Surveyor General extensive powers to refer subdivision proposals to the Townships Board and he has been described as a "watchdog of physical planning" (36). In consequence of the Housing Acts of 1937, 1944, 1945, 1957 and 1966 a Housing Commission exists which carries out housing schemes and planning layouts in connection therewith. The Railways Expropriation Act No. 37 of 1955 entitles the Railways to expropriate for housing and other railway purposes; and because the Railway Administration is a central government body it can completely disregard planning schemes drawn up by local authorities. The Group Areas Act No. 77 of 1957 (now replaced by Act 36 of 1966) and the related Community Development Act

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(34) See Chapter V at page 117.

(35) See page 43 above.

(36) See Bouchier op. cit. page 28.

No. 3 of 1966 have important planning implications (37). The Group Areas Act establishes a Board which is principally concerned with racial zoning and influences the siting of residential areas. Whilst its powers overlap with those of the Native Affairs Department under the Native Urban Areas Act No. 25 of 1945, they are broader because the Board is concerned with all residential areas in contrast with the Native Affairs Department which only concerns itself with residential areas for Bantu. The Advertising on Roads and Ribbon Development Act No. 21 of 1940 overlaps with the powers of local authorities with undesirable results. The Natural Resources Development Act No. 51 of 1947 established the Natural Resources Development Council which was given wide powers over the subdivision and development of land in areas declared under the Act. The Act was intended to be applied only to the undeveloped areas and did not have as its purpose the creation of a supreme controlling authority for physical planning. Other examples of legislation having a direct or indirect effect on planning are the Slums Act No. 53 of 1934, the Public Health Act No. 36 of 1919, the Deeds Registries Act No. 47 of 1937, the Water Act No. 54 of 1956 and the Factories' Act No. 28 of 1918.

That the central government is not unaware of the overlapping and confusion in the field of physical planning is apparent from the establishment in August 1964 of the Department of Planning. In November 1963 a government press notice stated: "... one of the great defects of the present planning service is the multitude of departments, divisions, councils performing planning functions on various levels of our hierarchy of authorities". The establishment of a national planning machinery was envisaged (38). One of the functions of the Department of Planning was to be the "co-ordination

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 (37) For discussion of the Community Development Act see below page 62 and Chapter IV page 94.

(38) See Roux "Town Planning - Shaping the Pattern of and Setting the Pace for Tomorrow's Urban Living", S.A. Treasurer of March 1968, page 81.

of all group areas, regional and physical planning with which the State may be concerned" (39).

To date significant accomplishment in the elimination of confusion in the planning field by the Department of Planning is not yet evident. Moreover, it may be debated whether the solution to the problem does not lie in the elimination of central government involvement in what is considered by some to be an essentially local government function. A further cause of confusion has been the Physical Planning and Utilisation of Resources Act No. 88 of 1967, which has the primary object of facilitating government control over the location of industry and places very wide discretionary powers in the Minister of Planning, enabling him to control the pattern of urbanisation to an important extent. At the present time it is not apparent how these functions will be exercised and what long-term influence on town planning they may have (40).

THE NATURE OF URBAN RENEWAL

Urban renewal is an integral part of city planning and not a distinct and separate activity. In the past planning relied upon the negative tool of zoning to control development; today through the use of urban renewal a more positive approach to control is becoming evident. Planning objectives are increasingly being attained not merely through the use of the police power of the State by means of zoning (41) but through the use of the State's power of expropriation. The most important asset of urban renewal is therefore the power of land assemblage through expropriation. The term 'urban renewal' is not easily defined. There is much confused thinking about the subject,

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(39) See Government Gazette 14th August 1964.

(40) See Chapter VII, page 175.

(41) See Chapter V below at page 109.

even on the part of the legislative bodies which have passed urban renewal enactments and the administrators whose task it is to carry out the provisions of these enactments. Perhaps the best definition attempted is that by Grebler:

"Urban renewal refers to a deliberate effort to change the urban environment through planned, large scale adjustment of existing city areas to present and future requirements for urban living and working. It extends to non-residential as well as residential land uses.

The process involves a re-planning and comprehensive re-development of land or the conservation and rehabilitation of areas which are threatened by blight or are to be preserved because of their historical setting and cultural values - all in the framework of an overall plan for a city's development. Because public as well as private improvements are required and because of the common difficulties of large-scale land assembly in built-up areas, urban renewal is characterised by substantial government action as well as by new private investment. The existence of a national programme, accompanied by financial and other assistance by the government, manifests a nation-wide interest in urban problems by far exceeding the earlier concern with poor housing.

The ingredients of governmental initiative and financial support, planning and large-scale enterprise distinguish urban renewal from the piecemeal replacement of structures, building by building, that has been going on for centuries. The close association with an overall-city plan, the inclusion of non-residential as well as residential land uses, and greater reliance on private investment distinguish urban renewal from the conventional slum-clearance and housing programmes"(42).

It is admitted by Grebler that this definition merely serves the purpose of distinguishing urban renewal from other processes that change the face and fabric of cities, and that the description of a process

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(42) Grebler, "Urban Renewal in European Countries: Its Emergence and Potentials", page 13.

does not suffice for a definition of its purpose (43). It is important to note from Grebler's definition that urban renewal is concerned with both redevelopment and rehabilitation (44). In the course of his study of urban renewal in European countries he found that its broad objectives were no more clearly defined there than in the United States and neither was its strategy in terms of programming, timing and priorities more highly developed (45). It is therefore not surprising that both in Europe and the United States urban renewal is a highly controversial subject and that much of what it attempts should be ill-considered and abortive. Some of its critics have gone so far as to call for its complete abandonment (46), but to require the patient's dispatch because he is possessed of ailments is an extreme prescription.

The basic aim of urban renewal in a free enterprise economy is to accelerate a private market process. The principal purpose of urban renewal in America has come to be the restoration of the vitality of the city, although it had its origins in housing legislation. Social and aesthetic factors enter into consideration, but the fundamental goals are economic and the main objective (rightly or wrongly) has become the return of business and population to the centre of the city. Urban renewal is directed at the removal of both the effects and the causes of urban decay. The two distinguishing characteristics of urban renewal (as compared to other redevelopment) in the United States are land assembly through expropriation and State

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(43) Op. cit. page 105.

(44) It is a thesis of Schaaf, op. cit., that the question of rehabilitation versus replacement is resolved solely on the basis of alternative costs (see page 7) and that through the enforcement of a code of minimum standards the criterion to be adopted is that of least-cost and not profitability (see page 8).

(45) Op. cit. page 104.

(46) See Anderson, "The Federal Bulldozer".

subsidy to fill the typical financial gap between the cost of acquiring land and the value of the sites which become available for use. Urban renewal in America has arisen principally through an enhanced understanding of the vital and unique function of the Central Business District and the complementary roles of the components of the metropolitan structure. The Central Business District has come to be recognised as being irreplaceable as the hub of business, professional, government and social activities. There are already indications that despite its critics urban renewal in the United States is beginning to achieve success. In the long term it will be helped by three important factors: the supply of suburban land well located for expansion is rapidly running out and is being further reduced by zoning restrictions; with the anticipated change in the demographic pattern, there will be a rapid rise in the 20-24 and over 55 age categories, thus increasing the demand for central city residential accommodation (47); freeway development is improving the accessibility of the Central Business District to and from the metropolitan area as a whole (although this may prove to be a two-edged sword). It would in fact appear that the exodus of the relatively affluent residents of the city has passed its peak (48).

Grebler found that European notions about urban renewal largely paralleled American. These included reduced density in built-up areas, more open spaces, the reproduction of some suburban amenities in central locations, a wider range of housing choices, ease of circulation, shorter journeys to work and the like (49).

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(47) See Whyte, "Changes in Metropolitan Areas", Appraisal Journal, July 1964, page 394.

(48) It should be noted that this exodus did not have the same effect on offices as it did on shops. This is because the locational requirements of shops and offices differ, the movement of retail trade being very largely related to residential movement.

(49) Op. cit. page 105.

He comments that from the point of view of the economist most European urban renewal seems to aim at the reduction of alleged or real diseconomies in the concentration of people and establishments, again a negative goal, instead of focusing on the optimisation of the 'external economies' which are the cities' *raison d'être*. Grebler found that the economic position of central cities in practically all European countries was much stronger than those in the United States because there had not been the same flight to the suburbs of the medium and upper income groups (50). The principal problems facing European cities were in fact traffic (including transit) and the need for additional space within the centre to perform central area functions. In addition the conservation of parts of the city of historical and cultural value also was cause for concern. At the time of his study, in early 1962, only four Western European nations had national urban renewal programmes going beyond the traditional slum clearance and housing schemes. These were France, Denmark, Great Britain and the Netherlands. However, in other countries urban renewal programmes were in the process of formulation and work on a local basis was proceeding (51).

THE NECESSITY FOR URBAN RENEWAL

There are a number of reasons why it may not be possible for private enterprise effectively to revitalise blighted areas without State assistance. The greatest obstacle is land assembly (52).

Without the use of expropriation it is frequently impossible to assemble land areas of adequate size because owners attempt to extort ransom prices for their properties and thus wreck the whole

(50) Op. cit. page 21.

(51) Stockholm's Nedre Norrmalm project, for example, was made possible by a special law. See Grebler op. cit. page 78.

(52) See above, page 38, footnote 10.

scheme. Often even if private development corporations were given the power of expropriation, the cost of land would exceed its value for redevelopment and State subsidy would be essential. Moreover, financial institutions are normally cautious about providing funds for redevelopment in blighted areas. Any development in a decayed area has usually to be of some scale to survive; an attempted improvement of an individual property is likely to be overwhelmed by surrounding blight.

THE SCALE OF URBAN RENEWAL

Although by 1965 more than 1,500 urban renewal projects were under way in the United States, urban decay was still outpacing redevelopment. It was considered that the urban renewal process would expand considerably and continue for an indefinite period of years. Urban renewal is not a device to provide public housing, but a tool for the redevelopment of large areas. It encompasses all the facets of municipal operations and is thought likely to become the single most important municipal activity. Co-ordination with other local government undertakings, such as freeway development, is essential. The nature of urban renewal is such that it is fundamentally a local and not a central government activity.

THE EXECUTION OF URBAN RENEWAL

It has become accepted policy in the United States that the expenditure of federal funds on urban renewal is appropriate because the vitality of the nation's cities is of concern to all its citizens. Nevertheless, the federal government has no power to enforce the programme. It offers help, including a two-third subsidy, to such local communities as wish to avail themselves of it, provided the local community commits itself to a 'workable programme'. In Britain the institutional framework of urban renewal is similar to that in the U.S.A. Plans have to be approved by the central government, but urban renewal is essentially a municipal undertaking.

The implementation of an urban renewal scheme demands that the central government, the local authority and private enterprise work together in harness. In America after all the properties for the scheme have been acquired the land is almost invariably sold to private enterprise. The more socialist philosophies of Britain and certain other European countries are reflected in a greater disposition towards permanent public ownership. The usual practice in Britain is to grant a long lease to private developers after the land has been assembled, the public authority thus retaining long term control (53).

Once the land has been expropriated there is no necessity for it to remain in single ownership. The two methods of sale favoured in the United States are negotiations under competitive conditions, and fixed price bidding with competition on a design basis. In Britain it has been common practice to dispose of projects through 'competition by tender' - a method in which both land price (or land rent) and design are criteria. This procedure has little to recommend it because the award becomes confused, and strong objections have been raised against it. In both Britain and the United States the land is disposed of subject to conditions assuring compliance with the master development plan for the area.

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- (53) For a discussion of the pros and cons of private and public ownership of land see Burroughs, "Should Urban Land be Publicly Owned?" *Land Economics*, February 1966, page 10, and Lichfield "Land Nationalisation" in "Land Values" at page 107. See also Pennance op. cit. at pages 39 to 40 for a comment on the concept of "crownholds" introduced in Britain by the Land Commission Act 1967. Pennance loc. cit. writes: "The economic merits of a policy of widespread public or municipal ownership of land resources are largely illusory but there may be decisive demerits in it from the viewpoint of economic allocation of resources. One merit of having to make continual reference to the market is that the cost of alternatives sacrificed by adopting the given line of action is always brought to the fore. Where need to make such a reference is absent, say a piece of land is already in the ownership of the authority, there is a strong temptation to use it in a way that may be economically wasteful (although otherwise very desirable) simply because it was acquired 'cheap' years before."

It is a somewhat surprising fact that in the U.S.A. expropriation is employed with less inhibition than in any European country apart from Britain. Somewhat less surprisingly, the Americans show less concern about the re-accommodation of persons displaced by an urban renewal scheme. Grebler attributes the willingness of the United States to employ expropriation, as compared with the pooling and rearrangement of existing private property interests preferred in several continental countries, to the American proclivity for 'getting things done' (54). With regard to the re-housing of people moved by an urban renewal scheme he points out that the American attitude towards mobility is at variance with European tradition and that a society where the average tenure of a home is ten years is bound to view displacement as a minor misfortune (55).

THE CRITICISMS OF URBAN RENEWAL

If the principal purpose of urban renewal is the removal of blight, then the nature of blight should be understood. Davis and Whinston state that blight exists where:

1. strictly individual action does not result in development,
2. the co-ordination of decision-making via some means would result in redevelopment, and
3. the sum of benefits from renewal could exceed the sum of costs (56).

It follows from this definition that blight is not necessarily associated with the outward appearance of properties in any area. Nourse (57) seems to be incorrect in considering that if blight is defined in this way there is no reason for governmental subsidy of urban

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(54) Op. cit. page 80.

(55) Op. cit. page 87.

(56) Op. cit. page 59.

(57) "Economics of Urban Renewal", Land Economics, February 1966 page 66.

renewal; the benefits and costs with which the government should be concerned would be social rather than private and some subsidy would be justified in circumstances where social benefits exceeded social costs. If Davis and Whinston's definition is accepted, the removal of slums as such ceases to be an objective of urban renewal and it is quite possible that slum property may not even be blighted property. It may represent the optimum usage not only in terms of private benefits and costs but also of social benefits and costs (58). The validity of this proposition has not been commonly recognised in urban renewal which is extensively being used as a tool for slum clearance - principally it has been suggested because the sight of slums is aesthetically offensive to the governing classes (59). Several observers have maintained that urban renewal is not a cure for slums and that the only result of an urban renewal scheme is the creation of slums elsewhere (60). Because the poor cannot afford to pay higher rents unless accompanied by rent subsidy, urban renewal would only lead to a less efficient allocation of resources and worse housing conditions than previously existed, for those removed from the area of the renewal scheme would be forced to bear a higher rent, or to pay increased transport costs, or to accept inferior accommodation (61). In the view of Thompson, the urban renewal programme in the U.S.A. has had an excessively physical bias because it has been conducted principally by persons who are not trained in economics. He states that the road to slum clearance should begin with the physical and mental health of the slum-dwellers and proceed to

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 (58) In any event, as Schaaf has pointed out, op. cit. at page 18, slums do not occur by accident and the cost of their elimination must be absorbed by someone.

(59) See Thompson, "A Preface to Urban Economics", page 126. Breger in "Concept of Urban Blight", Land Economics, November 1967, page 371, states that "non-acceptance is the fundamental signification (i.e. test) of urban blight."

(60) See Davis and Whinston, op. cit. page 60.

(61) See Nourse, op. cit. page 69.

education, productivity and income (62). He observes that the economist viewing the urban renewal programme in the United States feels a little uneasy because "one does not plant better houses and neighbourhoods to grow better households but rather one implants better skills, aspirations and opportunities to grow better houses and neighbourhoods" (63). Nourse (64) points out that improved housing does not have many of the social benefits which were at one time attributed to it.

Thus far urban renewal projects in the United States have indeed had an extremely adverse effect on the inhabitants of slums. The average rent that they have to pay for accommodation to which they have moved has been considerably higher without any improvement at all in the quality (65). In consequence of the renewal programme there has been a reduction in the supply of lower rent housing (66). In reality while it is one of the prime purposes of urban renewal to improve housing conditions for the lower income group it has in fact worsened them for this group and improved them for the higher income group. Between 60 per cent and 70 per cent of those forced out of their homes by the urban renewal programme in the United States have been members of the non-White group (67). Private enterprise, in contrast to urban renewal, has achieved a remarkable improvement in housing standards in the United States. In the decade 1950-1960 the percentage of sub-standard units of the national occupied stock

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(62) Op. cit. page 127.

(63) Op. cit. page 222.

(64) Op. cit. page 64.

(65) Anderson, op. cit. page 62.

(66) Anderson, op. cit. page 65.

(67) Anderson, op. cit. page 213.

dropped from 35 per cent to only 17 per cent (68) and even non-White housing enjoyed a very considerable increase in quality. These results were achieved with virtually no assistance from the federal urban renewal programme. A material factor in the improvement of the housing for the lower income groups having been the movement of the higher income groups to the suburbs (69), it is debatable whether the efforts which the urban renewal programme is making to obtain a return of wealth to the centre of the towns is in the social interest (70). The repeated assertions that slums are spreading is attributable to the fact that although sub-standard structures are being vacated they remain standing and continue to despoil an ever-increasing portion of the landscape (71).

It has been maintained that urban renewal does not increase the demand for accommodation and therefore its principal effect is to alter the location of constructional activities in a city rather than the volume of such activity (72). It is a fact that urban renewal projects have generally not been profitable for private enterprise and that considerable difficulty has often been experienced in disposing

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- (68) Grigsby, "Housing Markets and Public Policy", reprinted in "Urban Renewal : the Record and the Controversy", page 31. These facts indicate that the view expressed by Schaaf in 1960, op. cit. page 1, that privately initiated renewal may not even reduce appreciably the number of sub-standard units is incorrect.
 - (69) Grigsby, op. cit. page 36.
 - (70) Grigsby, op. cit. page 37; Grigsby: "A General Strategy for Urban Renewal", reprinted in "Urban Renewal; the Record and the Controversy", page 661.
 - (71) Grigsby, op. cit. page 32.
 - (72) Smith, "The Federal Bulldozer : A Review", reprinted in "Urban Renewal: the Record and the Controversy", page 534.

of land after it has been assembled (73).

The most fundamental criticism of urban renewal is its infringement of personal liberty. Grebler (74) writes:

"Perhaps no single activity affecting city life epitomises the conflict between the rights of the individual and the powers of the state as much as does an urban renewal programme ... In urban renewal the conflict between the state and the individual extends not only to definition of private property rights but also to the often painful dislocation of large numbers of people, businesses and institutions, and it may involve the dissolution of some of the social fabric of a city."

It is of the utmost importance that in the consideration of town planning generally and urban renewal especially, more careful examination should be given to the concept of the social or community interest. It is suggested that the community is nothing more than the aggregation of the private citizens who constitute it and that if it is seen to be such, infringement of liberty will be minimised. The concept of the community is certainly not to be permitted to become equated with the pleasure of bureaucracy (75). Moreover, the danger of a concept such as that postulated by Hegel, which conceives the community as an entity apart from and above private citizens, is disastrously evidenced by the pre-war development in Italy and Germany of Neo-Hegelian philosophy which became overwhelmingly directed to the glorification of the State as the

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(73) See Anderson, op. cit. page 11; Kay, "The Industrial Corporation in Urban Renewal", reprinted in "Urban Renewal: The Record and the Controversy", page 284.

(74) Op. cit. page 76.

(75) Day op. cit. page 104 uninhibitedly equates the "community" with the "local authority".

embodiment of the aspirations of the Nation (76).

URBAN RENEWAL IN SOUTH AFRICA

Legislation was passed in South Africa in 1965 in which the term 'an urban renewal scheme' appears (77). The Government has taken comprehensive powers, but neither the Act itself nor the debates in Parliament which preceded it give much indication of the manner in which these will be administered. Some doubt as to the purpose of the legislation has arisen through its being brought to the Statute Book as an amendment to the Group Areas Development Act No. 69 of 1955 (78). It would, in the writer's view, have been better embodied in an Act passed specifically for this purpose.

The powers the central government now has to implement urban renewal include the right of expropriation (79), the right to freeze development (80), the right of pre-emption (81), the right to control usage (82), the right to override town planning schemes (83) and ordinances passed by provincial administrations and by-laws by

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- (76) See Friedmann, "Legal Theory", 3rd Edition, page 95. Consideration should also be given to experience in the Communist-controlled countries of Europe.
- (77) Community Development Amendment Act No. 44, 1965, Section 5.
- (78) The short title of this Act was changed to "Community Development Act 1955" by Act No. 44 of 1965. Together with its amendments it has now been consolidated in the Community Development Act No. 3 of 1966.
- (79) Section 38 (1) (a). See Chapter IV below page 98.
- (80) Section 15 (2) (e).
- (81) Section 15 (5) and Section 30 (1).
- (82) Section 15 (2) (e).
- (83) Section 20 (2).

municipalities (84), the right to make loans (85), and the right to make ex gratia grants (86). The urban renewal programme is administered by the Community Development Board under the relevant Minister. Urban renewal seems to be envisaged as a central government rather than a local government function; the participation of private enterprise was not discussed when the Bill was debated in Parliament.

It has been stated above that in Britain and in the United States urban renewal is essentially local in character and its execution is predominantly through private enterprise. As the concept of urban renewal has grown away from mere slum clearance, it has become necessary to relate urban renewal projects to the overall development plans for the city. In similar manner greater reliance has come to be placed upon private enterprise. The powers the Government in South Africa has taken to disregard town planning schemes and to freeze property are regrettable. The former constitutes an undesirable interference in local government, and the latter conflicts with the basic function of urban renewal, namely to prime the pump of private enterprise. The need for urban renewal legislation is undoubted; what is uncertain at present is the manner in which the Government intends that it should be implemented.

COST-BENEFIT ANALYSIS

In the private sector cost-benefit analysis is the accepted and normal technique for the evaluation of any proposed investment. It is concerned only with private costs and benefits and is relatively simple in its application because the costs and benefits with which it has to do can be meaningfully reduced to money terms and are normally not too remote to be quantified. When the social costs and

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(84) Section 20 (2).

(85) Section 15 (2) (f) (iv).

(86) Section 15 (2) (c).

benefits of a proposed activity have to be assessed a problem is usually posed which is more complex and less capable of precise solution than where the analysis is concerned only with private costs and benefits. Nevertheless, the basic techniques for evaluating proposed undertakings in the private and public sectors are the same. In the field of town planning cost-benefit analysis is still in its infancy, the literature on the subject is limited, and the nature of the problems which arise is such that the quantification of benefits, and to a lesser extent of costs, is often highly subjective. Moreover, it is still comparatively rare for the techniques of cost-benefit analysis to be applied to planning proposals and the writer knows of no single occasion where this has been done in South Africa (87). Despite this circumstance, it is submitted that for all the limitations in the accuracy of cost-benefit analysis in the town planning field it should be applied to all major planning decisions.

The essential principle of cost-benefit analysis is that which was postulated at the outset of this chapter, namely that any expenditure (whether it be in the private or public sector) should produce a marginal benefit which is at least equal to the marginal benefit which could have been obtained by some other expenditure. In the

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- (87) A reviewer of a study by Lichfield entitled "Cost Benefit in Town Planning - A Case Study of Cambridge" believes that the exercise described therein was the first practical application in Great Britain of the technique to a particular planning problem. See Chartered Surveyor, February, 1968, at page 146. A further published study by Lichfield is "Cost Benefit Analysis in Town Planning - a case study : Severley", Urban Studies, November 1966. Lichfield in "Cost Benefit Analysis in Town Planning" Estates Gazette October 19, 1968, at page 275 has subsequently stated that the technique has now "been applied in practice to a wide range of town and regional planning problems". Peters, "Cost Benefit Analysis and Public Expenditure" at page 36, questions the validity of Lichfield's approach because he doubts whether it is possible to avoid "dressing up prejudices".

absence of the observation of this principle, there is no rational system by which the scarce resources of the community can be allocated (88).

Lichfield (89) has developed the elements of a system of accounting in order to record social costs and benefits arising in the planning field. The more closely the situation to be examined in the public sector resembles situations which arise in the private sector, the more easily can the problem be reduced to financial terms. For example, money values can be attached with greater facility to a

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(88) See Barlowe, "Land Resource Economics", pages 483 - 492. Pennance op. cit. at page 29/30 writes: "No doubt planners, in common with most other forms of publicly financed activity, would, if they could, prefer to insulate themselves from the need to fight all other contenders for public funds. But if insulation is achieved only by disguising the true cost in terms of foregone alternatives which planning decisions impose on the community, it is unlikely to produce rational economic decisions on the best use of resources. For example, if planners wish to take land from a use upon which the market places a certain value and put it to a lower order use (say, by reducing the density of development or preserving it for an open space) then, from the viewpoint of society's economic welfare, nothing is gained by allowing them to obtain it cheaply. They are merely encouraged to use it wastefully, with less regard to sacrificed alternatives. If particular planning activities, whether positive or restrictive, are considered worthwhile on any rational economic calculus of benefit and cost, they should be undertaken. If they are not considered worthwhile on this basis, nothing is gained by adopting a misleading economic calculus to get a desired answer". Peters, op. cit. page 9, states: "Attempt must therefore be made to investigate methods of analysis which facilitate and rationalise public decision making. The central problem is that of 'priorities', a shorthand term for the criteria of allocating resources between competing uses in the absence of markets. Confident claims are constantly being made about the desirability of this or that government action, but it is evident that a large part of public spending is voted on the basis of hunch, guesswork, horse-trading or barely concealed electoral calculations."

(89) See Lichfield, "Cost Benefit Analysis in City Planning", Journal of the American Institute of Planners, November, 1960, page 273, and Lichfield, "Cost Benefit Analysis in Planned Evaluation", Town Planning Review, July 1964, page 158.

proposal for the employment of expropriation in order to assemble a site where this end is being frustrated by monopoly, than to a proposal that an area of land be declared a green belt. The criteria to be employed in the first problem closely resemble those of the market; the criteria in the second problem are more remote from the market, perhaps not in terms of costs but certainly of benefits. In the first case the benefits to the private developer to whom the assembled land is sold at its market value will roughly equate the social benefits (90); in the second case the amenity arising to the community from the green belt can hardly be priced, but nevertheless its cost can be compared with the cost of alternative expenditure in the process of deciding how resources should be allocated. It follows that the mere discipline of attempting to quantify social benefits and costs will serve an enormously useful function in clarifying the ends to which the community decides to devote its limited means. More than one system attempting to classify the more immediate and more remote social costs and benefits resulting from an undertaking has been devised. The terminology is consequently somewhat confusing. The first problem is that of enumerating the costs and benefits which flow from an undertaking, and the second, that of evaluating these; the more remote (and the more intangible) they are, the more difficult will be both their identification and their quantification (91). Prest and Turvey put forward the following formulation:

"The aim (of cost benefit analysis) is to maximise the present value of all benefits less that of all costs, subject to specified constraints"(92)."

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- (90) It being noted that social benefits have been defined above to include the benefit flowing to the private developer from his undertaking. See page 158 above.
- (91) See Prest and Turvey, "Cost Benefit Analysis: A Survey", *Economic Journal*, December, 1965, page 683; "Traffic in Towns", Her Majesty's Stationery Office, 1963, Appendix 2.
- (92) *Op. cit.* page 686.

From this formulation it follows that the costs and benefits and constraints have to be identified, that costs and benefits have to be valued and that interest rates have to be established at which these valuations will be discounted to bring them to their present value (93).

The technique of cost-benefit analysis can be seen to be a useful discipline in public expenditure, but a tool which will be the more imperfect the less firmly its particular application is based upon individual preferences as revealed by the operation of the market. It is not a panacea to the problems of economic planning and it is not to be abused by being used to cloak planning decisions with the trappings of scientific objectivity in circumstances where the figures employed are essentially subjective. Rather, cost-benefit analysis should serve as a cogent reminder of the extreme difficulty of making decisions where the market is either not able to provide requisite goods and services or is not permitted to do so (94).

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(93) On the question of the choice of interest rate see Prest and Turvey op. cit. pages 697-700. It is to be noted where there are two or more mutually exclusive projects, that having the most favourable cost-benefit ratio will not necessarily be the most desirable. A discussion of this problem falls beyond the scope of this chapter. For its solution see Merrett and Sykes, "The Finance and Analysis of Capital Projects", Ch. 5.

(94) West, "The Future Pattern of Ownership and Development of Property", Estates Gazette, December 7, 1968 page 1091, comments as follows:

"The main hazard to planning is that it has to be based upon forecasts - economic, industrial, social, population, and so on. These forecasts are bound to be fallible and many of them in the past have proved to be ill-founded - for example, planning up to the 1940's was based largely on the assumption that we were to have a diminishing population in this country in the second half of this century. In the 1950's and 1960's planning has to some extent been based upon preventing a drift to the south-east, although the Registrar General's statistics show that this was probably mythical; nevertheless it is a difficult concept to remove from the minds of the planners, and if the policy turns out to have been founded on a wrong assessment, it may be that the particular region will have suffered a serious blow. It may be that we should be following the examples of the 'economic miracle' countries and be encouraging industrial growth anywhere, irrespective of immediate social and political theories."

CHAPTER IV

COMPENSATION UPON EXPROPRIATION

INTRODUCTION

In the Roman State there was no restriction upon the power of the supreme legislature and it could therefore expropriate for any purpose, although in practice this power was used sparingly and with hesitation (1). Roman-Dutch law recognised the power of expropriation subject to the payment of compensation (2). There is in South Africa a plethora of statutory enactments providing for expropriation. Whilst these vary greatly, they would generally appear to have been influenced by and in some cases modelled on English law. Mr Justice Schreiner in *Rigg v. S.A.R. & H.* (3), after discussing the English Lands Clauses Consolidation Act, 1845 (4), and the Natal Lands Clauses Consolidation Law, 1872 (5), stated: 'The resemblances between the English and Natal provisions on the one hand and section 7 (of the Railway Expropriation Act, 1955) on the other, are noteworthy and make it highly probable that the

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(1) See W.W. Buckland and A.D. McNair, "Roman Law and Common Law", 2nd Edition (revised by F.H. Lawson 1965), pp.95 ff.

(2) See A.S. de Blécourt, "Kort Begrip van het Oud-Vaderlands Burgerlijk Recht", 7th Edition (by H.F.W.D. Fischer, 1959), page 164.

(3) 1958 (4) S.A. 339 (A.D.).

(4) 8 & 9 Vict., c. 18. The Lands Clauses Consolidation Act, 1845, may be regarded as the basis of the present English system of expropriation. See Lawrance and Chavasse, "Compulsory Purchase and Compensation", 2nd Edition, page 3.

(5) Law No. 16 of 1872.

scheme and much of the wording of the latter is derived from one or both of the earlier statutes' (6).

It is believed that the underlying principle of expropriation ought to be that a person whose property is taken should be financially as well off after such taking as before (7). Compensation should enable the owner to replace the property taken by other property which will have the same pecuniary value to him. The question is not what the taker has gained but what the owner has lost. The main purpose of the discussion in this chapter is to examine the extent to which this principle is observed in practice.

THE ADMINISTRATIVE AND THE JUDICIAL DECREE METHODS

There are two general types of expropriation procedure: the administrative method and the judicial decree method (8). The administrative method is used in England and has been adopted in South Africa, but is not widely employed in the United States. In fact some State constitutions in the U.S.A. have provisions preventing its use.

Under the administrative method title passes immediately to the expropriating authority, and an owner who refuses to accept the compensation offered is compelled to institute judicial proceedings. In the judicial decree method title does not pass until the amount of compensation is settled and paid, and the burden of bringing an action in the event of disagreement rests with the authority.

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(6) At 346.

(7) This was described as the "principle of equivalence" by Lord Justice Scott in *Horn v. Sunderland Corporation* (1941) 2 KB.26 at 49.

(8) For a general discussion of these two methods see Rokes, "An Analysis of Property Valuation Systems under Eminent Domain".

Despite the fact that when there is disagreement about compensation it may be months before payment is received, under the administrative method the authority can usually dispossess the owner at short notice. Most property owners cannot afford substitute accommodation whilst their assets are frozen pending the outcome of a court case and few can risk the expense of an unsuccessful action. The administrative method is clearly weighted heavily against the property owner and he is frequently forced to settle on terms favourable to the expropriating authority. Such advantage as may accrue to the community through the avoidance of any delay in the implementation of public works by the use of the administrative method has little significance when compared with the inequity caused to the expropriated owner. It is to be hoped that the various expropriation enactments in South Africa which embody this method will be amended and to be regretted that the opportunity to do so was not taken when the Expropriation Act of 1965 (9) was passed.

MARKET VALUE OR VALUE TO THE USER? (10)

Courts have frequently held that compensation is to be paid at market value, which they have defined as the price which a willing buyer would pay and a willing seller would accept (11). The concept of market value is dependent upon the notion of the hypothetical 'typical' purchaser (12). It is clear that the value of a property

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- (9) Act No. 55 of 1965. For a discussion of this Act see below page 89.
 - (10) For a discussion of these concepts see above Chapter II pages 6 and 11.
 - (11) Pietermaritzburg Corporation v. South African Breweries, Ltd., 1911 A.D. 501 at 515-16; Durban Corporation v. Lewis, 1942 N.P.D. 24 at 49; Colyvas v. Valuation Court, Pretoria, 1960 (4) S.A. 34 (T) page 40; Margate Hotel (Pty) Ltd. v. Town Council of the Borough of Margate, 1961 (1) S.A. 384 (N) at 388; but see Salisbury Portland Cement Co., Ltd. v. Edwards Timber and Lime Industries (Pvt.) Ltd., 1962 (2) S.A. 167 (S.R.) at 174.
 - (12) Salisbury Portland Cement Co., Ltd. v. Edwards Timber and Lime Industries (Pvt.) Ltd., 1962 (2) S.A. 167 (S.R.) at 174.

to a particular owner is identical in amount with the entire financial loss direct and indirect that the owner would suffer if he were to be deprived of the property (13). It is equally apparent that real estate, unlike toothpaste or any other fungible, is a commodity which can have more financial worth to its owner than to any other person. The question arises whether in expropriation valuations a distinction should be made between the market value of the property and the pecuniary value of the property to the particular owner. Unless a special construction is placed upon the term 'market value' in expropriation cases, the concept will fall short when applied to the value of a church, a school, a specialised industrial building or any other property for which the selling price on the open market is likely to be less than the pecuniary value of the property to the present owner. For this reason, Orgel (14) maintains that the proper measure of just compensation is the market value of the property or the value of the property to the owner, whichever is the greater.

Bonbright (15) writes:

"When the market value of a property at the time of taking is the accepted measure of compensation, value in a hypothetical market and not actual market value, must necessarily be accepted in order to avoid circuitry of reasoning. At the time of taking, which corresponds roughly at least to the time when the owner is deprived of the beneficial use of the property, the condemned property is literally valueless, both to the owner and to any prospective private owner, except for the fact that its ownership confers a claim to a money compensation from the condemnor."

Because the market under consideration in an expropriation case is

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(13) Bonbright, "Valuation of Property", 1937, I, page 71.

(14) "Valuation under Eminent Domain", cited in Appraisal Journal, April 1960, page 194.

(15) Op. cit., page 414.

only hypothetical (16), it is possible and reasonable to assume the existence of hypothetical purchasers for whom the property will be as well suited as for the owner. The assumption must be made that there are willing purchasers in the hypothetical market who would want the property for the purpose for which it is being used by the owner. In an expropriation case, the market value of a church ought not to be determined by asking what the ordinary citizen, who has no desire to acquire a church, would give for that piece of property, but what a congregation who wish to buy a church would give for it. Thus the measure of compensation in the case of expropriation cannot be distinguished from the pecuniary value of the property to the particular owner. The inequity of any other approach is manifest.

It is therefore apparent that the term 'market value' can be interpreted strictly or liberally. Equity demands a liberal interpretation, but it is necessary to consider whether this has in fact been accepted by South African courts. In the leading valuation case of Pietermaritzburg Corporation v. South African Breweries, Ltd. (17), Mr Justice Jacob de Villiers said:

"The word 'value' as pointed out by writers on Political Economy, has two meanings. It sometimes expresses the utility of some particular object (which is called value in use) and sometimes the power of purchasing other goods which is its value in exchange (Mill, Pol. Econ., Bk. II, ch. 1) When the legislature prescribes that the value of the property has to be determined, it refers to the exchange value of the property, in other words, the amount of money for which the property can be exchanged or sold" (18).

While it is strange that the Court should have turned to Mill for

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(16) See Salisbury Portland Cement Co., Ltd. v. Edwards Timber and Lime Industries (Pvt.) Ltd., 1962 (2) S.A. 167 (S.R.) at 174.

(17) 1911 A.D. 501.

(18) At 522.

guidance when Marshall's "Principles of Economics" had already reached its sixth edition by 1910, and although no economist today would accept without qualification the statement that value in use or value to the owner expresses the utility of a thing, nevertheless the distinction drawn between the value of a thing to its owner and the price at which it can be sold is fundamental and correct. What is questionable is the further statement in the judgment that selling price should be the test of value (19). It is submitted that the mind of the Court was not applied to the problem which has been posed here. The Pietermaritzburg case was concerned with an assessment for rating purposes, and a valuation which ignored the special value of the property to the owner would not have done injustice to any individual.

In the judgment in Krause v. S.A.R. & H. (20) the following words of Lord Dunedin in the English case of Corrie v. MacDermott (21) were cited but were not essential to the decision which was reached: 'The value which has to be assessed is the value to the old owner who parts with his property' (22). On the other hand, in the case of Raja Vyricherla Narayana Gajapatiraju v. Revenue Divisional Officer, Vizagapatam (23) the Privy Council held: 'It is often said that it is the value of the land to the vendor that has to be estimated. This, however, is not in strictness accurate. The land, for instance, may have for the vendor a sentimental value far in excess of its "market value". But the compensation must not be

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(19) Expressly adopted by Innes J. at 515.

(20) 1948 (4) S.A. 554 (0) at 561.

(21) (1914) A.C. 1056 (P.C.) at 1062.

(22) It should be noted that under the Lands Clauses Act the basis of compensation was value to the owner, but the Acquisition of Land (Assessment of Compensation) Act, 1919 (9 & 10 Geo. V, c. 57), changed the basis to market value. See R.C. FitzGerald, "The Law and Ethics of Compulsory Acquisition of Land" (1952) "5 Current Legal Problems" page 55 at page 75.

(23) (1939) A.C. 302 (P.C.). See, also, I.R.C. v. Clay and Buchanan (1914) 3 K.B. 466 (C.A.).

increased by reason of any such consideration (24). In the Natal case of Durban Corporation v. Lewis (25), the Court cited and approved the passage quoted from the Raja case. Mr Justice Broome stated: "Many of the English authorities . . . say that value means value to the owner, and that market value is not a conclusive test of real value. It is this view that, in my opinion, is responsible for the confusion to which I have already referred" (26).

With respect, it is precisely the failure to observe the view that Mr Justice Broome criticises that has led to confusion. 'Real value' is a myth which economists have long abandoned and which the judiciary would do well to jettison (27). However, in Natal, at least, the question is decided until such time as the Appellate Division has opportunity to overrule Durban Corporation v. Lewis. If our courts could be persuaded to use the liberal interpretation of 'market value', the allowance of special value to the owner would not be abused, because the burden of proof of establishing the value of his property lies upon the owner (28), and it would certainly be very heavy where any large sum were claimed for special value. In any event the value to the owner cannot exceed the cost of equivalent substitute premises with due allowance for expenses and losses incurred in moving (29). Moreover, when property is held purely for investment purposes, there is no difference between strict market value and value to the owner. Consequently, special value to the owner has only to be estimated where the property is occupied by the

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(24) Per Lord Romer at 312.

(25) 1942 N.P.D. 24.

(26) At 48.

(27) See below page 82 and Chapter II page 6.

(28) Die Suid-Afrikaanse Naturelletrust v. Kitchener, 1964 (3) S.A. 417 (A.D.).

(29) See Chapter II page 11.

owner himself (30). The Privy Council's mention of 'sentimental value' in the passage quoted from the Raja case above is inapt. The analysis is directed entirely towards the pecuniary loss of the owner. It may be that this failure on the part of the courts to understand that the special value to the owner has a very genuine financial significance explains their reluctance to interpret 'market value' liberally. It seems possible that when judges have made a distinction between 'market value' and 'value to the owner', they have been concerned with the additional value to the owner arising from sentiment and not from the cost of acquiring an equivalent property. Any property which has a peculiar suitability for a particular use is likely to have a higher substitution cost than the price it would fetch if it were sold on the open market.

The English Land Compensation Act, 1961 (31), re-enacting previous legislation with slight amendments, provides six basic rules (32):

Rule 1 - No allowance shall be made on account of the acquisition being compulsory.

Rule 2 - The value of land shall, subject as hereinafter provided, be taken to be the amount which the land if sold in the open market by a willing seller might be expected to realise.

Rule 3 - The special suitability or adaptability of land for any purpose shall not be taken into account if that purpose is a purpose to which it could be applied only in pursuance of statutory powers, or for which there is no market apart from the special needs of a particular purchaser or the requirements of any authority possessing compulsory purchase powers.

Rule 4 - Where the value of the land is increased by reason of the

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(30) If a property had special value to a tenant and the contract rent were less than the value to the tenant, this would have to be taken into account in assessing the compensation payable to the tenant. See discussion page 86.

(31) 9 & 10 Eliz. II, c. 33.

(32) See Lawrance, Rees and Britton, "Modern Methods of Valuation", 5th Edition, pp. 333 ff.

use thereof or of any premises thereon in a manner which could be restrained by any court, or is contrary to law, or is detrimental to the health of the occupants of the premises or to the public health, the amount of that increase shall not be taken into account.

Rule 5 - Where land is, and but for the compulsory acquisition would continue to be, devoted to a purpose of such a nature that there is no general demand or market for land for that purpose, the compensation may, if the Lands Tribunal is satisfied that reinstatement in some other place is bona fide intended, be assessed on the basis of the reasonable cost of equivalent reinstatement.

Rule 6 - The provisions of rule 2 shall not affect the assessment of compensation for disturbance or any other matter not directly based on the value of land.

It is submitted that Orgel's view that compensation should be the higher of market value or value to the owner (33) provides a more logical approach to the matter for which allowance is made in rules 2, 5 and 6 (34). Rule 4 is so obviously correct that it does not need to be discussed. FitzGerald (35) questions the fairness of rule 1 and observes that previously when statutory undertakers expropriated land under the Lands Clauses Acts a sum of 10 per cent was always added. The present writer does not feel the rule to be unjust. With regard to rule 3, it is submitted that this is unfair to the extent that the public authority could reasonably be regarded as being part of the normal market for the property. It should be noted that wording similar to that of rules 1, 3 and 4 is commonly to be found in expropriation legislation in Britain and

(33) See above, page 71.

(34) See comment on the unsatisfactory operation of these rules in a memorandum entitled "Compensation for Compulsory Acquisition and Planning Restriction" submitted to the British Ministry of Housing and Local Government by the Chartered Land Societies Committee in 1968.

(35) Op. cit., pp. 66-7.

other countries (e.g. the Railway Expropriation Act, 1955 (36), in South Africa).

SEVERANCE DAMAGE

We turn now to circumstances where property is taken in part only and the financial loss to the owner exceeds the value of the part taken, i.e. where severance damage occurs. Severance damage is the loss in value of the portion remaining. In *Durban Corporation v. Lewis* (37) the Court had to interpret the following words of the Natal Lands Clauses Consolidation Law, 1872: 'In estimating ... compensation ... regard shall be had ... not only to the value of the land ... taken .. but also to the damage ... to be sustained by the owner ... by reason of severing the lands taken from the other lands of such owner, or otherwise injuriously affecting such other lands' (38). It was held (39) that the owner was entitled to receive as compensation: (a) the value of the land taken (including buildings), (b) the damage sustained in regard to other land and (c) the damage (including the loss of business) sustained generally by reason of the expropriation of land. The amount under each head, it was held, should be assessed separately. It was observed in *Illovo Sugar Estates, Ltd. v. S.A.R. & H.* (40) that the 'only case in South Africa in which these sections, or similar sections in other legislation, have been considered is *Durban Corporation v. Lewis*'. To the best of the writer's knowledge this position still prevails as far as severance damage is concerned (a problem with which the court was not concerned in the *Illovo* case). It appears to be the

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(36) Act No. 37 of 1955 Section 6(4).

(37) 1942 N.P.D. 24.

(38) Act No. 16 of 1872, sec. 41.

(39) Per Broome J. (as he then was) at 47. Hathorn J.P. concurred.

(40) 1947 (1) S.A. 58 (D) at 56.

view of Dönges and Van Winsen (41) that the judgment in *Durban Corporation v. Lewis* represents the correct method of assessment of severance damages in terms of the common law.

The rule that each head of damage has to be assessed separately presents the valuer with grave difficulties. There is no logical basis on which such an assessment can be made. Fortunately other legislation (e.g. the Railway Expropriation Act, 1955 (42)) has adopted the realistic rule that compensation should be based on the 'before and after' method. Under this method the compensation awarded is the difference between the value of the entire property before taking and the value of the remainder after taking. Whilst it may be possible to estimate the value of a part taken in isolation, it is not possible to calculate severance damage other than by the 'before and after' method. The results of an attempt to estimate severance damage in any other way would be arbitrary.

The discussion in Chapter II above on the difficulty of estimating 'depreciation' in any other way than by reference to market value is relevant, because severance damage is nothing other than the depreciation suffered by the remainder of the property in consequence of the expropriation of a part. Where law compels a valuer to make separate estimates for compensation for the part taken and compensation for severance damage, he will first employ the 'before and after' method and, having arrived at a figure, he will proceed to apportion this as between compensation for land taken and compensation for severance to the remaining land (43). No purpose would be served by thus separately valuing the portion to be taken except in circumstances where legislation (for reasons not apparent to the

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(41) "Municipal Law", 2nd Edition (1953), page 366.

(42) Act No. 37 of 1955. Vide sec. 6(2).

(43) See Lawrance, Rees and Britton, op. cit., pp. 394-5.

writer) places restrictions upon the amount of compensation in respect of the portion taken (e.g. the Cape Municipal Ordinance, 1951 (44)).

The basic tests which should be applied by the courts are:

- (a) Is the part that is purportedly 'severed' a portion of an integrated whole with the part that has actually been taken?
- (b) Has the value of the part that is purportedly 'severed' decreased?

The vital question is whether the unit value of the remainder is reduced as a result of the taking. In the English case of *Duke of Buccleuch v. Metropolitan Board of Works* (45) it was held that dust, noise and loss of privacy likely to arise from the use of land for a public road were good grounds for compensation where the land affected was held with that acquired. Examples of other circumstances which might be taken into account in awarding severance damages are:

- (a) loss of access to remainder;
- (b) irregular shape of remainder;
- (c) small area of remainder;
- (d) shallow depth of remainder;
- (e) prevention of most effective plan of subdivision;
- (f) adverse effect on drainage of remainder;
- (g) placing a burden on the remainder by necessitating expenditure on fences, re-erection of building, etc.; and
- (h) preventing full use of remainder for a period (46).

.....
(44) Ord. No. 19 of 1951. Vide sec. 137(2). See discussion below at page 92.

(45) (1872) L.R. 5 H.L. 418.

(46) See McMichael, "Appraising Manual", 4th Edition, page 438.

CONSEQUENTIAL DAMAGE

It was noted above that it was held in *Durban Corporation v. Lewis* (47) that damages should be assessed under three heads, the third being the damage (including loss of business) sustained generally by reason of expropriation of land. The damages contemplated under this head are presumed to relate not to the property itself but to other loss consequent upon the taking, such as moving expenses, loss of goodwill and the like. The Court specifically ruled that among the factors to be taken into account was the possibility that "the owner may suffer damage by being unable to trade for a period" (48). The Expropriation Act, 1965 (49), appears to make specific provision for such consequential damage (50). A consideration of this type of damage is beyond the scope of this discussion, which is limited to the loss from expropriation bearing upon land and buildings.

WHEN MUST THE WHOLE BE TAKEN?

The next problem to be considered is whether when an authority wishes to acquire a portion of an area occupied by a building, it can be compelled to acquire the entire area occupied by the building. Section 92 of the English Lands Clauses Consolidation Act of 1845 provided: 'No party shall at any time be required to sell or convey to the promoters of the undertaking a part only of any house or other building, if such party be willing and able to sell and convey the whole thereof.' The interpretation which the English courts have placed on the words 'house' and 'building' serves to clarify the

(47) 1942 N.P.D. 24.

(48) At 47.

(49) Act No. 55 of 1965. See discussion below, page 89.

(50) Sec. 8(1) (a) (ii).

meaning of those words in South African legislation (51). Halsbury states: 'By a house or building is meant more than the mere fabric. The word house includes the house, garden, and curtilage, in fact all that would pass on conveyance of the house' (52). In order to modify the operation of section 92 and reduce the inconvenience caused to public authorities through their being forced to acquire property surplus to their needs, modern expropriation legislation based upon the Lands Clauses Consolidation Act has usually embodied a 'material detriment' clause. In South Africa, for example, section 7(1) of the Railway Expropriation Act (53) is to the effect that no person can be compelled to part with only a portion of any building unless in the opinion of the court such portion can be severed from the whole without material detriment thereto. The court will have to take into account the physical consequences of the expropriation of only a part of a building and the effect on the unit value of what remains after taking (54). Lawrance, Rees and Britton (55) state that if the loss of the part can fairly be met by payment of reasonable compensation there can be little doubt of the acquiring body's right to take a part only under a 'material detriment' clause, but where the part of the property which is left is physically incapable of reinstatement or amendment so as to render it fit for the type of use and occupation formerly enjoyed by the owner, or where the damage is so great that any compensation sufficient to meet the loss to the owner would be out of proportion to the total value of the property, the owner is clearly justified in claiming that the whole should be taken. It seems probable that

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(51) e.g. sec. 7(1) of the Railway Expropriation Act, No. 37 of 1955.

(52) "Laws of England", 3rd Edition, X, 110, page 70.

(53) Act No. 37 of 1955.

(54) Sec. 7(2) provides specifically for compulsory acquisition of a remainder of less than one acre. Vide *Rigg v. S.A.R. & H.*, 1958 (4) S.A. 339 (A.D.).

(55) Op. cit., pages 324-5.

this statement also correctly expresses South African law.

TEMPORARY OR INTRINSIC VALUE?

We now turn to the question whether property should be valued at its 'temporary' or at its 'intrinsic' value. It should be noted that the market value of property (56) is defined at the moment in time when the valuation is made. In *Pietermaritzburg Corporation v. South African Breweries, Ltd.* (57), Mr Justice Jacob de Villiers stated:

'It remains to consider whether this exchange value is the temporary or market value of the property or whether it is what has been called its permanent or natural value, to which market value after every variation tends to return. In the absence of any provision to the contrary, I am of the opinion we must take the word "value" in its ordinary meaning of temporary or market value' (58). In *Katzoff v. Glaser* (59) it was similarly held: 'The real object of search is "the temporary or market value" which may fluctuate to different levels at different times and vary as the mood of the general buying public is sanguine, pessimistic or apathetic' (60). Thus the valuator is not required to attempt to stabilise the value over a period. The concept of 'natural', 'permanent', 'real' or 'intrinsic' value fails to recognise that 'value' is a factor of supply and demand. Indeed, in practice it would be impossible for the valuator to adopt any value other than the one at a particular time, because it cannot be prophesied with reasonable accuracy what market conditions will prevail in future. This does not result in injustice to owners of property, because although they may receive lower sums of compensation

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(56) See Chapter II above, page 6.

(57) 1911 A.D. 501.

(58) At 522.

(59) 1948 (4) S.A. 630 (T); but see *Durban Rent Board v. Edgemount Investments, Ltd.*, 1946 A.D. 962 at 973.

(60) At 638, per Dowling J.

in times of recession than in times of boom, they are also able to purchase substitute accommodation more cheaply. However, where valuation is dated back to a time of recession but actual compensation paid in a rising market, the owner may be severely prejudiced. A partial solution to this problem would seem to be that sums of compensation should be adjusted to allow for inflation between the date of expropriation and the payment of compensation.

ADMISSIBLE EVIDENCE

In the United States the assessment of property for rates, being made for another purpose and not at the instance of either party, and not usually at the market value of the property, is not admissible as evidence of value in condemnation proceedings (61). Our own courts could hardly adopt this attitude, however commendable it may be, because in certain instances Parliament has actually referred them to rating assessments as a guide to value, for instance, the Income Tax Act, 1962 (62), and Rents Act, 1950 (63). Indeed a curious provision of the Cape Municipal Ordinance, 1951, actually forbids an arbitrator to grant compensation in excess of the rating assessment except in certain restricted circumstances (64).

The use of the reproduction cost or summation method of appraising

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- (61) San Jose & A.R. Co. v. Mayne, 83 Cal. 566, quoted in McMichael's "Appraising Manual", 4th Edition, page 451; Thies, 'The Law of Eminent Domain: Its Origin and Development', Appraisal Journal, 1957, page 59.
- (62) Act No. 58 of 1962, sec. 62(5).
- (63) Act No. 43 of 1950, sec.1(xiii).
- (64) Ord. No. 19 of 1951, sec. 137. See below, page 92.

finds little favour with courts in the United States (65), except where the buildings are of a specialised or institutional nature. The attitude of our own courts is similar. In *Pietermaritzburg Corporation v. South African Breweries, Ltd.* (66) it was stated that 'the present cost of erecting a building bears no necessary relation to the market value of the building' (67).

Valuations made for fire insurance purposes are not admissible evidence in expropriation cases in the United States (68). This rule is so clearly correct that it would surely be followed by a South African court.

The valuation must not be based on allegedly comparable sales which are too remote in time. Whilst there is no certain yardstick on this point, the circumstances of the market for the particular kind of property will provide an idea of what is reasonable. In the United States there are cases which have held that three years is too remote and others which have held that eight years is not too remote (69).

.....
(65) See following cases cited in *Appraisal Journal*, 1960, pages 384, 386:

1. *State v. Red Wing Laundry and Dry Cleaning Company*, 93 N.W. 2d 206, in which the Minnesota Supreme Court held that the summation method 'is not to be taken in derogation of the unit rule of valuing property as a whole'.
2. *Carlstrom v. United States*, 275 N.W. 2d 802, in which the United States Court of Appeal stated: 'Reproduction cost is not the best evidence of fair market value if other evidence is available'.
3. *United States v. Certain Interests in Property*, 271 F. 2d 379, in which the United States Court of Appeal took the view that the summation method generally is held to be one of the least reliable indicia of market value'.

(66) 1911 A.D. 501.

(67) Per De Villiers J.P. at 524.

(68) Vide Thies, op. cit., note 61 above.

(69) Thies, op. cit.

In the United States if at the date of taking there is a reasonable probability (70) of a change in zoning within a reasonable time, the influence of this circumstance on market value may be shown (71). The test is not the value that the property would have if the zoning were changed but the effect on the market value at the time of taking of the prospect of beneficial zoning amendment. Evidence may be led of the value the property would have after change only in order to demonstrate the effect of the prospect of change upon the present market value. No matter how probable a zoning amendment appears, some doubt remains and influences present market value. It is to be noted that the purpose of zoning is to encourage the optimum utilisation of land resources in social and economic terms (72), that evidence may be led to show that an existing zoning does not provide for the optimum land usage, and that such evidence will demonstrate the likelihood of zoning amendment. It would be an abuse of the powers of a public authority to refuse to rezone land merely because that public authority had an interest in the acquisition of the land and wished to minimise the costs of purchase (73).

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- (70) In some judgments the term 'reasonable possibility' is used. See *State of New Jersey v. Gorga*, 133 A. 2d 349, 138 A. 2d 833, quoted in "Condemnation Appraisal Practice", published by American Institute of Real Estate Appraisers, page 88; *United States v. Meadow Brook Club* 259 F. 2d 41, quoted in *Appraisal Journal*, Jan., 1962, page 58.
 - (71) South African courts have held similarly. See Chapter VII below and in particular the discussion of the rating cases of *Geldenhuis v. Johannesburg Municipality* 1917 T.P.D. 241 and *Kleinfontein Estate v. Benoni Municipality* 1918 T.P.D. 193, and the expropriation cases of *S.A. Railways v. New Silverton Estate Limited* (1946) A.D. 830 and *Krause v. S.A.R. & H.* (1948) (4) SA. 554 (O).
 - (72) See Chapter III pages 36-38.
 - (73) See "Condemnation Appraisal Practice", pages 41-5, 87-9; J.F. Rowlson, 'Zoning vs. Alternate Value', *Appraisal Journal*, Oct., 1963, pages 513 ff.; E.C. Fisher, 'Zoning in Eminent Domain - A Moral Hazard', *Appraisal Journal*, July, 1965, pages 331 ff.; B.R. Stottle, 'Reasonable Probability - Exception to the Rule', *Appraisal Journal*, Jan., 1962, pages 55 ff.

WHAT INTERESTS MUST BE COMPENSATED?

In England the Lands Clauses Consolidation Act, 1845 (74), so defines the word 'lands' as to extend compensation to lessees, sublessees and other persons having an interest in land. The holder of an option to purchase the land has been held to be entitled to claim compensation (75). A legal right to renew a lease provides a claim for compensation (76), but the mere possibility that the lease may be renewed does not (77). In terms of section 18, separate notice has to be served on all the parties interested in the land. The position in the United States would generally appear to be similar (78). Under the judicial decree method all interested parties have to be made defendants so that they may be heard upon the gross amount of damages to be awarded (79). The gross amount will be the aggregate of the damages in respect of the various separate interests. It follows from what has been said above (80) that the compensation to be paid to a lessee should be the present value of the difference between the rent under the lease and the value of the premises to the lessee.

In South Africa, regrettably, the position of the holders of interests other than the freehold is less satisfactory. It has been held (81) that unless a statute specifically provides for compensation to lessees, a lessee cannot claim compensation from the expropriating authority. Parliament and the provincial councils appear to

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(74) Sec. 3.

(75) *Oppenheimer v. Minister of Transport* (1942) 1 K.B. 242.

(76) *Bogg v. Midland Railway Company* (1867) L.R. 4 Eq. 310.

(77) *Ex parte Nadin* (1848) 17 L.J. Ch. 421.

(78) See "Condemnation Appraisal Practice", published by the American Institute of Real Estate Appraisers, pages 397-442.

(79) *Ibid.*, page 408.

(80) Pages 73-75.

(81) *Trustee of Kimberley Public Gardens v. Colonial Government* (1887) 5 S.C. 316.

have attached an unwarranted significance to the registration of rights, and South African enactments typically provide that compensation will only be paid in respect of such rights as are recorded on title deeds (82). It is, it is submitted, quite unthinkable that the holders of unregistered rights (which would include rights acquired by prescription) should be put to the trouble and expense of having these rights registered (assuming that the holder of the freehold or of any other registered interest did not oppose such measure) because of the remote possibility that a property might be expropriated. Moreover, holders of unregistered rights (which may well have more value than the rights of the freeholder) should not only have a right to compensation, but also a right to receive notice of expropriation and to appear in any court action. Dison and Mohamed (83) state on the authority of Pothier (84) that common law will not normally entitle a lessee to claim damages from the owner when he is ejected in pursuance of an expropriation (85). Whatever claim a tenant may have on grounds of unjust enrichment against an owner who receives compensation upon expropriation could hardly be considered a satisfactory remedy (86). The point

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- (82) For example, the Expropriation Act, No. 55 of 1965, secs. 1(v), 8(4) (e) and 13; the Community Development Act, No. 3 of 1966, sec. 1(1) (xviii). The Cape Municipal Ordinance, No. 19 of 1951, is somewhat exceptional in that it does make provision for a purchaser who has not yet received title to share in the apportionment of compensation (sec. 135) and includes in the definition of a right in respect of land certain unregistered interests (sec. 126). The Railways Expropriation Act, No. 37 of 1955, does not limit compensation to the holders of registered rights, see below.
 - (83) "Group Areas and their Development" (1960), page 123.
 - (84) "Contrat de louage", 87.
 - (85) It should be noted that in Stellenbosch Divisional Council v. Shapiro, 1953 (3) S.A. 418 (C) which held that the doctrine of 'huur gaat voor koop' was not applicable in expropriation, the Court was concerned with the tenant's rights to remain in occupation and not with his right to compensation.
 - (86) If the owner were insolvent the tenant would presumably only be a concurrent creditor.

is more than academic because in practice leases frequently have a definite capital value to tenants (87).

FOUR IMPORTANT ENACTMENTS

We turn now to a more detailed examination of four important examples of South African legislation:

(a) The Railway Expropriation Act (88)

The Railway Expropriation Act of 1955 replaced the varying provincial enactments (89) under which expropriation for railway purposes had previously been made. This Act appears to have been modelled upon the English Lands Clauses Consolidation Act, 1845, and Acquisition of Land (Assessment of Compensation) Act, 1919. It provides in section 6(1) that compensation shall be paid for any property expropriated, or in respect of any right or interest in or over land which has been injuriously affected, or any other loss or damage sustained. It is laid down in section 6(2) that the 'before and after' method shall be used in the assessment of severance damage. The normal provision is made to exclude allowance on account of the owner's having been deprived of the property without his consent or on account of the special usefulness of the property for the purposes for which it is being expropriated (90). The wording of section 6(4)(c), which provides that no allowance shall be made

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(87) In particular, it is common practice for holding companies to let property to subsidiary companies at rents below the level a subsidiary would have to pay to a landlord to whom it was not a subsidiary.

(88) Act No. 37 of 1955.

(89) The Railway Expropriation of Lands Ord., No. 20 of 1903 (T); Act No. 10 of 1899 (N) and the Railway Improvement Act, No. 27 of 1904 (N); Railway Construction (Special Powers) Ord., No. 30 of 1903 (O); Railway Expropriation of Lands Ord., No. 46 of 1903 (O).

(90) Sec. 6(4) (a) and (b). See above, page 75.

for any 'indirect damage', is not easily reconciled with the provision in section 6(1) that compensation will be paid for 'any other loss or damage sustained'. Presumably the intent of section 6(4)(c) is merely to place a test of remoteness on loss.

(b) The Expropriation Act (91)

The Expropriation Act of 1965 amended a number of Acts containing expropriation clauses (92) and provided an alternative procedure to all remaining expropriation legislation other than the Railway Expropriation Act, 1955 (93). It is to be regretted that expropriation provisions in terms of group areas, slums and housing statutes and the Cape Municipal Ordinance escaped amendment, and to be hoped that the authorities concerned in each case will employ the procedure under the Expropriation Act and not continue to use the old enactments. It is also unfortunate that the opportunity was not taken to provide the owners of quit-rent land in the Cape with the right to receive compensation when their land is expropriated for road purposes. The exclusion of such right may have had some justification in 1813 (94), but today it is quite unrealistic and inequitable. As Pigou (95) has said, reasonable expectation is a more fundamental thing than legal right. In introducing the Bill to Parliament, the Deputy Minister of Lands stated that he anticipated the legislation would ultimately be used for all expropriation purposes (96). It

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(91) Act No. 55 of 1965.

(92) Vide secs. 18-36 of the Act.

(93) Sec. 17.

(94) The date of the Cradock Proclamation establishing quit-rent tenure in the Cape Colony.

(95) 'Principles of Compensation' in "A Study of Public Finance", 3rd Edition page 12.

(96) House of Assembly Debates, vol. 14, cols. 5056, 5141 (29th and 30th April, 1965).

ought to be noted that it is available as an expropriation instrument not only to Central Government departments but also to local authorities (97).

In a number of respects the provisions of the Expropriation Act, 1965, closely resemble those of the Railway Expropriation Act, 1955. The essential provisions for compensation are similar. But the Expropriation Act does not make specific provision for the 'before and after' method in the calculation of severance damages. This is an unfortunate omission as it may lead to doubt about the manner in which severance damages are to be assessed. Further uncertainty will be created by the non-inclusion of a clause similar to section 7(1) of the Railway Expropriation Act, whereby an owner who suffers material detriment through partial taking can compel an authority to take the whole of the property. The explanation for the legislature's failure to abide by a well-tried model is not obvious. The Act lays down that compensation shall be equal to market price plus an amount to compensate for any actual pecuniary loss or inconvenience caused by the expropriation (98). However, a similar problem to that arising under the Railway Expropriation Act again exists, because it is provided that no allowance shall be made for any indirect damage (99). The allowance for interest on compensation as from the date of expropriation is welcome, although it is regrettable that the rate is subject to the control of the Minister of Lands, whose department may well be an interested party (100).

The objectives for which the Act may be used to expropriate are defined in the broadest terms: 'for public purposes'. In African Farms

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(97) Sec. 15.

(98) Sec. 8(1).

(99) Sec. 8(4)(e).

(100) Sec. 8(2).

and Townships, Ltd. v. Cape Town Municipality (101) the Court was required to interpret the phrase 'public purposes' in item 19 of the Second Schedule of the Financial Relations Consolidation and Amendment Act, 1945 (102). Watermeyer J. held (103): 'There is no suggestion in item 19 that after expropriation the land should be used by the expropriating authority for public purposes. The true enquiry under item 19 is what is the respondent's object in expropriating. Dealing with the meaning of the expression "public purposes", Innes J.A. pointed out at page 283 (of Rondebosch Municipal Council v. Trustees of the Western Province Agricultural Society, 1911 A.D. 271) that the word "public" is one of wide significance and in a broad sense it is commonly applied to things which pertain to or affect the people of a country or a local community. In that sense public purposes are purposes which pertain to and benefit the public in contradistinction to private individuals.'

Similarly in Slabbert v. Minister van Lande (104) Claassen J. decided that the words 'public purposes' must be contrasted with 'private and/or personal purposes', and upheld an expropriation on the ground that it embraced the characteristics of a public purpose rather than those of a private or personal purpose (105).

It is to be wondered whether the courts will accept the Act as a tool for urban renewal. If not, urban renewal expropriation will have to be made under the Community Development Act, 1966 (106).

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- (101) 1961 (3) S.A. 392 (C).
 - (102) Act No. 38 of 1945.
 - (103) At 396-7.
 - (104) 1963 (3) S.A. 620 (T).
 - (105) At 622.
 - (106) Act No. 3 of 1966. See Chapter III page 62.

(c) The Cape Municipal Ordinance (107)

The Cape Municipal Ordinance, 1951, is an unhappy enactment in so far as its expropriation provisions are concerned. In terms of section 129, a council may within its municipality expropriate land for all municipal purposes. Once a council has served notice of expropriation upon an owner it must attempt to negotiate the amount of compensation. Only when agreement cannot be reached does it become necessary to appoint an arbitrator (108). The case where compensation is settled by agreement and the case where it is fixed by an arbitrator must be distinguished because in the latter circumstance the Ordinance places a limitation on the amount of compensation (109).

In terms of section 137(2)(a), the compensation that the arbitrator can award in respect of expropriated land may not exceed the municipal valuation of the expropriated land by more than 30 per cent. It is submitted that this limitation refers only to the first head of compensation as laid down in *Durban Corporation v. Lewis* (110), and that there is no limitation on the compensation which may be paid for severance or for general damages sustained. As indicated above (111), the valuer has to arrive first at a figure for compensation by the 'before and after' method and he then has to apportion it as between the land taken and the remaining land. To the extent that the value of the part taken exceeds the municipal valuation thereof by more than 30 per cent, the owner will suffer a financial loss. This interpretation appears to accord with the

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(107) Ord. No. 19 of 1951.

(108) Sec. 136(1).

(109) Sec. 137.

(110) See above, page 77.

(111) Page 78.

view of Dönges and Van Winsen (112). As has been observed above (113), in the United States the assessment of property for rates is not admissible as evidence of value in expropriation proceedings. Moreover, rating assessments under the Cape Valuation Ordinance, 1944 (114), are based upon the summation method, the unsatisfactory nature of which was discussed in Chapter II above. The Cape Municipal Ordinance does not indicate the general principles according to which compensation must be determined, although it quite unnecessarily draws the valuer's attention to an absurdly incomplete list of factors which must be taken into account.

The reason why in terms of section 137(2)(a) the arbitrator should have to consider the 'average price at which land in the neighbourhood of the expropriated land has been sold' is obscure, for values may vary greatly in a neighbourhood. It is also difficult to see any real reason why only sales by 'public auction' should be considered. This is a comparatively uncommon method of selling property in South Africa and is frequently quite unsuitable if the highest price is to be achieved. It should be noted that Mr Justice Caney in *Margate Hotel (Pty.) Ltd. v. Town Council of the Borough of Margate* (115) specifically excluded sales by auction in defining market value. Thus, the curious circumstance exists that what is laid down as a norm by the Cape Provincial Council is rejected as a test of market value by a Natal judge.

(d) The Community Development Act (116)

We proceed to an examination of valuation under the Community Development Act, 1966 (originally passed in 1955 and described until a-

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(112) Op. cit., pages 365 ff.

(113) Page 83.

(114) Ord. No. 26 of 1944, sec. 43, as amended by Ords. Nos. 7 of 1956, 22 of 1959, 8 of 1960, 18 of 1961, 15 of 1965 and 8 of 1966.

(115) 1961 (1) S.A. 384 (N) at 388.

(116) Act No. 3 of 1966; previously Act No. 69 of 1955, as amended by Acts Nos. 81 of 1959, 23 of 1961, 49 of 1962, 80 of 1964, 44 of 1965, 42 of 1967 and 58 of 1968.

mended in 1965 as the Group Areas Development Act, 1955). The purpose of this statute is to develop group areas and to discourage speculation in consequence of the implementation of group areas. It contains provisions for the expropriation of property and for the limitation of either loss or gain by property owners. The term 'affected property' covers properties which are owned or occupied by members of a racial group who have to move from an area in terms of a proclamation under the Group Areas Act, 1966 (117).

The Group Areas Development Act, 1955, established the Group Areas Development Board (118) in order to control the sale of affected property, to develop group areas, and to assist persons to purchase and hire property in group areas in relation to which they were not disqualified (119).

The 'basic value' of every affected property has to be determined and is defined as the market value of the land immediately prior to the basic date plus the estimated cost of erection of the building on the land as at the time of valuation, less depreciation due to wear and tear and to the unsuitability of the building for the purpose for which it is being used (120). The 'basic date' is the date of publication in the Government Gazette of the proclamation by virtue of which the property became affected (121). The proviso was added by the Group Areas Development Act, 1959 (122) that the

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(117) Act No. 36 of 1966. This is subject to the qualifications in sec. 1(3) of the Community Development Act.

(118) Now renamed the Community Development Board.

(119) Vide sec. 2 of Act No. 69 of 1955, now sec. 15 of Act No. 3 of 1966.

(120) Sec. 1(1)(iii).

(121) Sec. 1(1)(ii).

(122) Act No. 81 of 1959.

basic value of the building should not in any case exceed the difference between the market value of the land determined on the basis that the building constitutes an integral part of the land, and the market value that the land would have if the building had not existed (123).

The underlying principles of the Act (references are to the consolidated statute of 1966) are the following:

- (a) When an affected property is sold for more than its basic value after the expiry of 60 months from the basic date, the seller must pay to the Board an appreciation contribution of 25 per cent of the difference between the sale price and the basic value (124),
- (b) when an affected property is sold for less than its basic value, the Board must pay to the seller a depreciation contribution of 80 per cent of the difference between the sale price and the basic value (125).

In terms of section 1(1)(iii) the market value of the land has to be taken immediately prior to the basic date and the cost of erection of the building has to be estimated at the time of the valuation thereof. Previously, as the writer pointed out in an article in the South African Law Journal in May 1966 (126), the proviso to section 1(1)(iii) (b) did not state at what date the second valuation,

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(123) Now sec. 1(1)(iii) of the 1966 Act.

(124) Sec. 34(4)(a). However if the disposition takes place after 72 months, the appreciation contribution is 50 per cent.

(125) Sec. 34(4)(b). The philosophy underlying these provisions would seem to be similar to that embodied in earlier British town planning legislation which attempted to compensate owners of land prejudiced by town planning and attempted to obtain betterment from those who benefitted. See Chapter V below, page 100.

(126) At page 201.

viz. that of land and buildings as a unit, is to be made. However, Act 42 of 1967 added words to the effect that the second valuation was to be made immediately prior to the basic date.

Because depreciation cannot be estimated without reference to market value (127), it follows that both formulae must produce the identical result if the valuation is made at the same date. Consequently, if the term 'depreciation' is to be understood in any normal sense, the cost of erection and the depreciation since erection would not need to be specifically regarded. However, the wording of the Act rules out such a simple approach. The valuation has to be conducted in part at the basic date and in part at a subsequent date, viz. the date of valuation. With regard to the first valuation, it should be noted that in practice the time lapse between the basic date and the date of valuation is likely to be considerable and that the change in supply and demand conditions (and hence in both land value and building value) may well be significant. One possible solution in the application of the Act appears to be as follows:

- (a) estimate value of land as at basic date;
- (b) estimate value of land as at time of valuation;
- (c) estimate value of property as a whole as at basic date;
- (d) deduct (b) from (c) to give value of buildings as at basic date;
- (e) add (a) to (d);
- (f) take lesser of (c) and (e) to be the value of the property.

This procedure seems so absurd that it is impossible to believe it to have been intended by the legislature. It is submitted that the only satisfactory approach is to estimate the value of the property as a whole as at the basic date and to take this to be the basic

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(127) See Chapter II above.

value without further ado. The wording of the Act may be attributable to failure by the legislature to understand the economic principles on which property valuation is based. It is interesting to note that in a comment on this submission published in the South African Financial Gazette (128), Mr J.H. Niemand, Secretary for Community Development, states that it

"...is in fact what is being done in practice with this difference, however, that the condition the buildings were in at the time of the valuation must be considered. The reasons are obvious. Departmental machinery can only come into motion after a list of affected properties has been compiled and valuers appointed. This inevitably takes time and in the meantime buildings may deteriorate considerably through the owner's neglect or may even be demolished. By the time the basic value can be determined, it may then not only be totally impossible for the valuers to determine what the condition and consequently the market value of a building was immediately prior to basic date, but it will furthermore be unreasonable and unrealistic to include in the basic value the value of a building as it was immediately prior to basic date whilst it had afterwards seriously deteriorated or had even been demolished."

It is submitted, however, that the possibility that buildings may be neglected is not a good reason for delaying the building valuation, because the point is covered by section 32(7), which provides for a reduction in value where after the determination of the basic value of land or buildings the value of such land has been reduced in consequence of, inter alia, neglect, damage, removal or destruction. Nor does the difficulty of finding evidence of the condition of the building at the basic date appear to be insuperable and hence justification for the postponement of the building valuation. Whatever practical problems may arise when a property has to be valued at a date in the past, they are as nothing compared to those which will be encountered if land and buildings have to be

.....
(128) 12th November, 1965, page 3.

valued on separate dates.

It should be noted that hypothetical market conditions must necessarily be assumed in estimating basic value (although the Act makes no specific allowance for this), because it is likely that many properties will become 'affected' by a proclamation in the Gazette, and if all had to be disposed of simultaneously, the average selling price would indeed be low.

The Community Development Board has the right to expropriate property, including that which has not become 'affected' by a proclamation (129). In respect of 'affected' property it also has a pre-emptive right (130). Other public authorities having expropriation powers for particular purposes of course may also expropriate 'affected' property. Whether 'affected' property is expropriated by the Board or by some other public authority, the 25/50 per cent appreciation and 80 per cent depreciation contributions discussed above are applicable (131). This is also the case where the Board exercises its pre-emptive right (132). Where the Board expropriates and agreement cannot be reached with the owner on the amount of compensation, it is specifically provided by section 41 that the compensation which the arbitrators may award (which is in any event subject to the appreciation and depreciation contributions) shall not exceed market value. Thus unless market value is interpreted liberally or an ex gratia payment is made by the State, it seems that the owner will not be compensated for such damage in excess of the selling price of his property as he may suffer. The legislature appears to consider that the value of a property is the sum of the separate values of its parts and to disregard severance damage altogether: section 35(3) provides that where a portion of an 'affected'

.....
(129) Sec. 38.

(130) Sec. 30.

(131) Sec. 35. and sec. 38.

(132) Sec. 34(4).

property is expropriated the basic value of the portion remaining shall be found by deducting the basic value of the portion taken from the basic value of the whole property.

In his work, "Land: Its Ownership and Occupation in South Africa" (133), Van Reenen wrote: 'At the very least it would seem that the whole question of affected properties and the determination of their basic values needs a complete and thorough revision.' This comment appears to have passed unheeded both when the Act was extensively amended in 1965 and when it was consolidated in 1966. One can but wonder how in practice valuers appointed by the Minister are carrying out their functions. The provisions of the Act relating to valuation are thoroughly unsatisfactory and ought to be amended at the earliest opportunity.

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(133) (1962), page 373.

CHAPTER V

THE COMPENSATION AND BETTERMENT PROBLEM IN TOWN PLANNING

PART 1 - GENERAL CONSIDERATIONS

The instruments of town planning, as we have seen in chapter 3, are public works (1) and usage restriction (2).

The promulgation of a zoning ordinance or the execution of public works will frequently adversely affect the value of some land and enhance the value of other land. Difficult practical and moral questions are posed; this chapter will discuss some of these problems and, in particular, attempt to assess the proposal advanced from time to time that a 'betterment' tax should be imposed upon land benefitted in order to compensate land prejudiced (3).

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- (1) including the assembly of land under urban renewal.
 - (2) A third instrument (which is not relevant to this discussion) might be thought to be the promotion by the State of statistical data and expert opinion in the field of land usage in order to facilitate the decisions of entrepreneurs, e.g. comparative data reflecting retail turnover within the Central Business District and suburbs and opinion as to the manner in which retail decentralization might be combated.
 - (3) British town planning legislation from 1909 to 1939 made a rough attempt to put this theory into practice. See Parker "The History of Compensation and Betterment since 1909" in "Land Values" at page 53. Other legislation which will be considered below might be thought to show more concern about the collection of betterment than the payment of compensation.

THE MEANING OF BETTERMENT

As Turvey has pointed out, the meaning of the word 'compensation' is clear, but the term 'betterment' is somewhat vague. To contrast 'compensation' with 'betterment' is confusing because the complement of compensation is not the betterment itself but charges levied in respect of it, while the complement of betterment might be called 'worsement' (4). Although the term betterment is sometimes broadly construed to mean an increase in land value due to community causes, this is not its normal use. The Uthwatt report in Britain defined betterment as "any increase in the value of land (including buildings thereon) arising from central or local government action, whether positive, e.g. by the execution of public works or improvements, or negative, e.g. by the imposition of restrictions on other land" (5).

RECOUPMENT

Betterment can accrue to the State in three ways: by recoupment, set-off and direct charge. Recoupment or excess condemnation is, as the latter term implies, the expropriation of more land than is needed for an undertaking with a view to its resale at a profit. In the U.S.A. several states have enacted constitutional amendments that expressly authorise recoupment and the courts in other states have accepted its use as legal when it appears reasonable (6). In Britain the power of recoupment has been given in various general Acts but has not been much used. There have, however, been many attempts under private Acts to recover betterment by recoupment (7).

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- (4) R. Turvey, "The Economics of Real Property", page 103.
- (5) Final report of the "Expert Committee on Compensation and Betterment" Cmd. 6386, 1942, para. 260.
- (6) Barlowe, "Land Resource Economics", page 523.
- (7) Lichfield, "The Economics of Planned Development", page 189.

It has not proved to be a financial success and has in some cases increased the total cost of a project (8).

SET-OFF

Set-off is a method of recovering betterment whereby the amount of compensation payable to the owner of expropriated land is reduced by the amount of any increase in the value of any other land belonging to him which can be attributed to works undertaken by a public authority. It should be noted that set-off refers to enhancement in the value of other land in proximity to the expropriated land and not to an increase in the unit value of the portion remaining where severance occurs because this would in any event be allowed for in the normal application of the 'before-and-after' valuation (9). Perhaps the most unsatisfactory feature of set-off is that it imposes a charge upon those persons some of whose property is being taken, but does not lead to contribution from the owners of other property in proximity to the expropriated property whose gain may well exceed that of the owners who have to pay set-off.

DIRECT CHARGES

In various countries at various times direct charges to recover 'betterment' have been levied both in respect of public action of a positive (public works) and of a negative nature (zoning). The question of whether such charges when made in respect of negative State action are justifiable is discussed below (10). Direct

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(8) Lichfield, op. cit. page 190: Turvey op. cit. page 109.

(9) See above Chapter IV, pages 77-79.

(10) See below pages 112-117 et seq.

charges made in respect of public action of a positive kind can be justified in so far as they constitute a method of distributing the cost of public improvements amongst owners who have benefited from them and the levy made upon any particular owner does not exceed the actual benefit to him. Unlike direct charges in respect of negative restrictions (which were first made in Britain in 1909), direct charges for positive action have an ancient history. Their first use in Britain was in 1427 in connection with sea defence work, but today they are not much used there except in certain local Acts (e.g. for the recovery of the cost of making private streets) (11). In the United States direct charges (referred to as special assessments) are widely used to finance the construction and provision of streets, sidewalks, drainage and the like (12). However, not all the costs which benefit an individual property are charged against the property by such assessments. These are only used when it is reasonably possible to allocate costs in accordance with benefit. Storm sewers, for example, may not be possible to finance in this way because of the problem of allocating costs (13). It may be that the circumstances in which direct charges are justified can be equated with those in which it is possible for the township developer to provide the services himself. It is in fact the policy in many areas in the United States to approve subdivisions only after the developer has provided satisfactory assurance that he is in a position to install and pay for the full range of services (14).

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(11) Lichfield, op. cit. page 336.

(12) Barlowe, op. cit. page 535.

(13) Ratcliff, "Real Estate Analysis", page 56.

(14) Ratcliff, op. cit. page 280.

THE 1947 ACT

The much debated Town and Country Planning Act of 1947 in Britain was tantamount to an adoption of the basic tenet of Henry George (15) that increases in land value due to communal causes should belong to the community as a whole. The objectives of the Act were both to secure for the community increments in land value and at the same time to compensate land owners, within certain severe limitations, for the loss of the development value of their land. Not only was betterment collected for publicly created increases in land value, but also in respect of increases arising from the owner's own efforts and to purely nominal appreciation consequent upon inflation. The development value of all land was nationalised and any person thereafter wishing to develop had to pay a development charge which represented the difference between the value of the land without permission to redevelop (described as 'existing use' value) and the value of the land with redevelopment consent. Previously in Britain the Finance (1909-10) Act 1910 had been inspired by a somewhat similar philosophy, but the 1947 Act dealt with the question of compensation and betterment on lines entirely different from any previous legislation. The Labour Government did not accept that owners were entitled to full compensation for their loss of development value, adopting the Uthwatt Committee's view that the property rights were "destroyed on the grounds that their existence is contrary to the national interest" (16). It should be noted that this is by no means the same concept as that in terms of which courts in the United States permit zoning without compensation in the interests of the 'general welfare' (17). The development charge provision of the 1947 Act proved impracticable and had to be repealed in 1953.

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(15) "Progress and Poverty". See Denman, "Land in the Market", page 32.

(16) Op. cit. paragraph 32.

(17) See page 109 below.

It did not wholly destroy the basis of the land market but substantially impeded its operation. Whilst the development charge failed to secure that property changed hands at existing use value, it affected the smoothness of the development process and retarded development (18). The charge removed the incentive of the owner to sell for redevelopment. Had it been less than 100 per cent this effect would have presumably been less severe (19).

FLOATING AND SHIFTING VALUE

Two concepts expounded by the Uthwatt Committee and embodied in the 1947 Act require to be discussed: floating value and shifting value. The Barlow Committee (20), which preceded the Uthwatt Committee, had correctly concluded that if the potential development value of each piece of land were assessed separately, the total sum arrived at would exceed the aggregate of the prices at which it would in fact be possible to sell the land. The Uthwatt Committee propounded the concept of a 'floating value' which once it settled on a site would cause other sites to lose their development potential. The Committee held that: "The 'global' method of valuation cannot assume, at the date on which the valuation is made, the possibility that demand will settle upon all units at that date. Therefore the 'global' valuation must be less than the aggregate of the individual valuations when considered separately" (21). This analysis errs in that it fails to recognise that value is a function of demand and supply, and that the supply of land for development at any time is not that land which has development potential, but only that which is offered for sale. Because the alternative value of a property

.....
(18) Lichfield, op. cit. page 345.

(19) For comment on the Land Commission Act 1967 in Britain see Appendix A below, page 124.

(20) Report of the Royal Commission on the Distribution of Industrial Population, Cmd. 6153 (1940).

(21) Op. cit. para. 23-24.

as an apartment site is higher than the value in its present use as a private dwelling, it does not follow that the owner wishes immediately to evacuate his home in order to conclude a transaction. The Uthwatt Committee took no account of the period over which properties with development value would be sold, and hence arrived at a basis of compensation which was completely unfair. If its premises had been correct, it would mean that the price of land for development is generally excessive, and this is manifestly not the case.

In the opinion of the Uthwatt Committee, town planning does not destroy land value, but only shifts it from one piece of land to another (22). This view requires to be questioned. The price mechanism operates to produce the optimum (23) allocation of land resources. To the extent that the functioning of the economy is not perfectly competitive or that planning leads to an allocation of land below optimum, land values can be destroyed and not merely shifted. It is indeed possible for planning to discourage entrepreneurial action with the consequence that a proposed land usage can be lost to a region or a country for all time. Such an event would cause a permanent loss of demand for land within that area with resultant loss in land values.

THE DIFFICULTY OF COLLECTING BETTERMENT

In practice it has proved difficult to find any equitable method of assessing betterment. It is not easy to distinguish between increases in land value which occur because of the manner in which an

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(22) Op. cit. page 15.

(23) In terms of economic efficiency but not necessarily social desirability. A purpose of town planning is to promote social goals which would not be achieved through the operation of the price mechanism, e.g. the prevention of ribbon shopping on major vehicular arteries or the preservation of historic buildings. See above Chapter III pages 35-39.

owner uses his land and those which can be attributed to community influences. As we have noted, the Town and Country Planning Act of 1947 in Britain did not attempt to make any distinction. In circumstances where legislation has provided that only betterment in a narrow sense (that arising from specific State action) may be collected, it has been found difficult to establish whether the increase in value has resulted from this or from betterment in a wider sense (that arising from increases in land value due to community causes). Nor can it easily be proved that betterment arises from a particular planning scheme. The radius of benefits following upon an undertaking may cover a considerable area and it may be hard to prove that one owner has benefitted more than another. Barlowe comments that in the United States special assessments frequently overcharge some owners and undercharge others (24). Moreover, a particular undertaking may benefit some owners but prejudice others. The construction of Charing Cross Road and Shaftesbury Avenue in London appears to have led to a rise in ground values of the frontage land and a fall in the value of property in adjoining streets (25). On the other hand, the construction of an expressway may well be of benefit to a neighbourhood as a whole but detrimental to the properties which have frontage on the new road. Weimer and Hoyt express the opinion that in the United States many special assessments should be abandoned because they are beneficial to motorists rather than property owners (26).

Betterment cannot be assessed until after an improvement has been carried out and some delay in its collection is therefore inevitable. Moreover, it is not practicable to demand its payment until the owner either wishes to redevelop or has sold the property. If immediate payment for betterment were demanded, an owner through

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(24) Op. cit. page 536.

(25) Turvey, op. cit. page 105.

(26) "Principles of Real Estate", 4th Edition, page 460.

lack of liquid resources might well be forced to dispose of his property. Consequent loss such as the ruin of a business could also result. Although the value of the property may rise over a period (or may rise and then fall), if a charge is to be made the betterment should be assessed immediately the improvement has been effected because the value at that moment in time will reflect the market's anticipation of future changes in value (27).

THE PAYMENT OF COMPENSATION

The compensation problems arising from 'injurious affection' through public works or loss in value through zoning are similar to those which have been considered in chapter IV on the actual expropriation of the title of a property by a public authority. In both cases the rights of the owner are taken to a greater or lesser extent and transferred to the public interest. The amount of compensation and the time at which it will be paid have to be determined. The mere publication of a planning proposal (indication of the possibility of expropriation or changes in zoning or the execution of either beneficial or detrimental public works) will affect the value of property and, if its terms are not precise, it is likely that more properties will be affected than will ultimately, for example, require expropriation for a new road. Compensation could be paid either when the fall in value occurs or when the actual loss takes place. If it were accepted that compensation should be paid when the value of the property fell, it would have to be decided whether this was the date on which the planning proposal became known, on which it received legal force, or on which it was applied to a specific property. If compensation were only payable when

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- (27) The value of any asset at any time is found by discounting predicted benefits (including amenities, income and re-sale price). If the assessment of betterment is delayed it is likely that some part of the benefit accruing to the owner from the improvement will already have passed and will escape the calculation.

actual loss arose this might be when the property was sold, when a mortgage bond holder demanded partial repayment because of decreased security, or when redevelopment consent was refused. As Turvey has pointed out, if compensation were known to be assessed at a level which would assure that no owner incurred financial loss there would be no problem because no fall in value would then occur (28).

The question of when a usage conflicts with the moral code of a society (and consequently when equity does not require compensation upon its restriction by zoning) is not capable of precise definition. The answer to the question is subjective and will alter as the moral standards of the community change. The problem has been stated more clearly in the United States, where the judiciary has been required to pronounce upon the limitations of the police power (29) of the State, than in Britain where the matter has rested with a Parliament holding power unfettered by a written constitution. The courts in America have permitted zoning without compensation provided that the provisions of legislation which the courts have not thought to fall within the police power have been permitted only if they provided for compensation. The analogy of the law of nuisance has been used by the judiciary to establish what legislation can be embraced by the police power, but through an evolutionary process much wider provisions have been permitted than fall under nuisance (30). It is permissible for zoning to take into consideration practices which bear no relation to the public health, safety or morals, but which come within the meaning of the broader term of

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(28) See Turvey, op. cit. generally pages 122-124.

(29) Note that the term "police power" is used throughout this work as it is understood in the United States, i.e. the power of the State to prohibit actions detrimental to public welfare.

(30) Barlowe, op. cit. pages 497-499; Ratcliff, op. cit. page 16; Mandelker, "Green Belts and Urban Growth", page 36.

'general welfare' (31). The precise meaning of that term will depend upon the interpretation of the courts which will inevitably be adapted to changes in the social conscience.

Zoning in Britain is less specific than is generally the case in the United States (or in South Africa). A development plan is drawn up to serve as a guide, but property owners must in every case apply for planning consent for a particular development. Lichfield states that with regard to existing buildings and existing uses the attitude of successive Parliaments has been fairly consistent in not permitting interference without compensation, but with regard to potential uses there has not been this consistency and different Acts of Parliament have decided the matter in different ways (32).

To the writer's mind compensation should always be assessed at the time a planning proposal is applied to a particular property, for example when it is rezoned for a less profitable use. Payment should follow forthwith upon assessment. If a property is detrimentally rezoned, the owner's capital loss is immediate and he should be immediately compensated. It is no argument against compensation that the owner did not in fact take advantage of the more valuable zoning whilst he was able to do so. There is no way of establishing when the owner might have sold or developed the property; there is every prospect that the owner had invested in the land with a view to development and paid the price set by the more favourable zoning; moreover, there is no obligation upon an owner to maximise the income produced by his assets. In Britain, because the detailed zoning system is not employed, it would only be practical to pay compensation when planning permission is actually refused. The amount of compensation would be the difference between the value of

.....
(31) Foss: "Interested Third Parties in Zoning". Appraisal Journal, January 1960, page 97 at page 103.

(32) Op. cit. pages 333-334.

the property with the prospect that it could be redeveloped (which in Britain would obviously be less than its actual redevelopment value) and its existing use value (33).

THE ECONOMIC INCIDENCE OF BETTERMENT

The person who has to bear the economic burden of a tax is not necessarily the person legally responsible for its payment (34). To the extent that work financed by a charge provides an owner with an amenity which the property otherwise would not have, the charge can lead to higher profits in the case of shops, factories, office and other productive property, and in the case of all property it can ultimately be passed to a purchaser; to the extent that the charge exceeds the increase in the value of the property the owner will receive no benefit from it.

BETTERMENT AND THE COST OF ACCOMMODATION

The pure theory of rent (35) holds that a charge imposed on land value will not affect the supply of land and hence will have no influence upon the cost of accommodation. In the realities of the market place there is not a fixed supply of land available for development; a charge which reduced the net price to a seller would decrease the quantity of land on offer at any moment and over time an undoubted result of a betterment charge would be to increase the

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(33) In actual fact the circumstances in which compensation can be recovered in Britain are severely restricted. See Mandelker, op. cit. pages 36 and 38; Lichfield, op. cit. page 346; Turvey, op. cit. page 144; Lawrance, Rees and Britton, "Modern Methods of Valuation", 5th Edition, page 301 et seq.

(34) See discussion below Chapter VI page 138.

(35) See discussion below Chapter VI page 132.

cost of accommodation (36).

WHO PAYS THE PUBLIC'S PIPER?

The question of compensation to individuals who suffer loss through town planning action is confused both in Britain and South Africa. The Uthwatt Committee found that the "history of the imposition of obligations without compensation has been to push that point progressively further on and to add to the list of requirements considered to be essential to the well-being of the community" (37). Lichfield aptly comments that "the cost of using land in the public interest has been transformed more and more into a private cost" (38). The evolution of the meaning that the courts in the United States have given to the police power in zoning reveals a not dissimilar position.

AN ATTEMPT TO STATE A GENERAL PRINCIPLE

In the view of Henry George (39), increases in the value of property which are attributable to the community as a whole and not to the owner should belong to the community and not to the owner. The contrary opinion holds that the prospect of gain or loss is part of the hazard of owning property, is allowed for in the price paid for property, and should rest (in the absence of State interference with

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(36) See Pennance "Housing, Town Planning and the Land Commission" page 43 et seq.

(37) Op. cit. paragraph 33.

(38) Op. cit. page 335.

(39) Loc. cit. See also J.S. Mill "Principles of Political Economy", Ashley's edition page 818.

benefit, but he has no right to expect payment (42). Similarly, in town planning the owner who is caused loss should receive compensation but the owner who receives a benefit which he has not requested should not be obliged to pay for it. A problem, less easy of solution, arises when an owner obtains a benefit for which he has asked such as a favourable change of zoning or permission to subdivide.

The answer to the question of when compensation ought to be paid is: whenever a zoning regulation is promulgated which does not constitute a reasonable exercise of the police power of the State. It follows that when the value of property is adversely affected by the amendment of zoning provisions relating to the property in terms of an established scheme, compensation must always be paid because it can hardly be held that the provisions of the town planning scheme in force are so contrary to the 'general welfare' as to merit the exercise of the State's police power. On the other hand if, for example, land is re-zoned to permit the erection of apartments and there is a fall in the value of land previously zoned for apartment purposes consequent upon the increase in the total supply of apartment-zoned land, this circumstance is part of the normal hazard of property ownership and no compensation should be paid.

We come now to the question of whether an owner should pay when he requests an amendment to a town planning scheme which will have the effect of increasing the value of his property. This would occur, for example, where demand existed for more intensive usage of the

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- (42) It could perhaps be argued that if you should subsequently sell the car at a price enhanced by the repainting it would be equitable for the painter to receive at least part of the benefit flowing from his efforts but the practical difficulty of identifying this gain is likely to be such as to make the principle unworkable. Note that the text attempts to draw an analogy between the equitable position of the car-owner and the land-owner and not to state the legal rights and obligations of the car-owner and the painter.

land and the owner asked for permission to subdivide or to erect a larger building. From time to time charges have been made by the State in circumstances such as these and have variously been referred to as betterment, special assessments, special rates, development charges and endowment. The theoretical bases for these charges have been one or both of the following:

- (a) because the value of a developer's land is increased he ought to pay to the State a charge representing the whole or part at least of the difference between the previous value of the property and its increased value;
- (b) the more intensive usage will place a burden on the capital investment of the community and ultimately necessitate an increase in its capital investment (e.g. dams, power stations, roads, schools, etc.).

The theoretical justifications put forward for charges of this nature are the product of confused thought. They err in assuming that the increased value of the land is essentially created by re-zoning. In actual fact the mere granting of permission to make more intensive use of land will, as we have seen (43), have no effect on its value unless there is a demand for the more intensive use. In towns which have no zoning scheme (a somewhat rare circumstance today) (44) the price mechanism will regulate the intensity of land usage. Communal causes will lead to increases and decreases in land value; more intensive usage will be possible or impracticable according to whether or not demand is sufficiently strong. This prospect of rise or fall in the value of land is one of the risks of

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(43) Page 113.

(44) Houston, Texas, is probably the largest town in the western world without zoning. See Olson, "Alternatives to Zoning - The Houston Story"; a paper delivered to the 1967 Annual National Planning Conference of the American Society of Planning Officials.

land ownership and is allowed for in the price paid for land (45). If a planning scheme is imposed on a community it does not have any necessary effect on land values. Within the limits set by the planning scheme the price mechanism continues to function as the regulator of the nature and intensity of land usage. Whether or not there is a town planning scheme the community will have acquired capital investments in dams and the like through the expenditure of funds raised by taxes of one form or another. The fact that a particular piece of land may have become ripe for township development will be attributable to the same communal causes whether or not there is a town planning scheme, although the promulgation of such a scheme may lead to some alteration in the actual areas which become ripe. The fact that land is ripe for more intensive use will be reflected in its value. That one piece of land has become so ripe and another not, is attributable to the fortune and foresight, or lack thereof, of the particular owner. By preventing a usage for which there is a demand the State can cause land to have a lower value than it would possess if the price mechanism were permitted to operate freely. If some charge is made for the enhancement in the actual value which occurs when the restriction is removed, this can only be in the form of confiscation of part of the value the property would enjoy when freed (46). If the value of the property were x when no charge was made, then when a charge is made the sum of the value of the property plus the charge will tend to be x also (47).

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(45) See below page 117. There is a frequent absence of understanding amongst writers on the subject of "betterment" that the price of land at any moment in time discounts prospective increases in value so that if the purchaser does enjoy a rise in value he gets nothing other than that for which he has paid.

(46) It being assumed that no compensation was paid when the restriction was originally imposed or that the subsequent rise in value exceeds the amount of compensation paid.

(47) To the extent that demand is driven to the property by unfavourable zoning elsewhere the amount x might exceed the value the property would have had if the operation of the market had not been disrupted by planning restrictions.

To the writer's mind, the disciples of Henry George have got in through the back door. What is described as a charge for the benefit of the planning permission is in reality a tax on the increased value of the land flowing from enhanced demand fundamentally attributable to communal causes and not re-zoning consent. It must be accepted either that changes in the value of land (48) are part of the risk assumed by the purchaser of land, or that the State should bear the hazard and not only charge land-owners who enjoy increases in land value but subsidize those whose land is reduced in value (a proposal which to the writer's knowledge has never been put into practice) (49). However, there is no objection to the State's insisting that the developer of land should be financially responsible for proper services which in the case of township subdivision might include roads, drainage, school sites, open spaces and the like, and in the case of an apartment might include adequate lifts, toilets, lighting and the like. To the extent that such costs may be embraced by a development charge made by the State, the charge is perfectly acceptable (provided the work undertaken by the State does not represent a usurpation of the functions of private enterprise) for the developer is merely being required to reimburse the State for undertaking functions which normally lie with the developer himself. It need hardly be said that zoning is a tool for town planning and not a weapon for raising tax, and that any proposed zoning amendment should be judged upon its planning merits and not influenced by some charge it might be possible to impose on the landowner (although if the theoretical premises of development charges

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- (48) Resulting from communal causes and not specific State action.
- (49) It is of interest that only one of the contributors to the colloquium reported in "Land Values", namely Colin Clark at pages 141-142, contemplates that land values might fall. The general assumption of the contributors seems to be that land values always rise.

were admitted they would have to be allowed for in any benefit-cost analysis) (50).

PART 2 - AN EXAMINATION OF THE SITUATION IN
THE FOUR PROVINCES OF SOUTH AFRICA

(a) Compensation

The Financial Relations Consolidation and Amendment Act No. 38 of 1945 (as amended) compels the provinces to pay compensation for any alteration to an existing subdivision or layout of land. Other matters are left to the discretion of the Provincial Councils (51).

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- (50) Denman, op. cit. at pages 33 to 34 writes: "Town and Country Planning controls are instruments designed to canalise the demands for proprietary interests in land in certain preconceived directions, in the interests of orderly development. Order is required to preserve or augment amenity, and prevent misuse and disarray. To the extent that these ends are achieved each citizen gets his just due - what he pays for in financing the planning authority. What just claim has he to cash bonuses in addition? We do not say of merchants and farmers whose fortunes are made by the public excise service that the increment should be paid to the community who provide the service. The landowner's decision is parallel." Floyd, "Town Planning in South Africa", writes at page 57: "It has been suggested that betterment should be enforced in the case of amending schemes.....The objection to this is that it leads to bargaining. Owners wanting a change of zoning will offer betterment to the local authority as a bait. Some councils may be tempted to agree in order to obtain the money and in this way much bad zoning may result. It is the author's opinion that planning or replanning should always be done on town planning merits only. Bargaining should be left out and if it is correct in the public interest to rezone, this should be done without payment."
- (51) Regrettably Parliament did not compel Provincial Councils to embody provisions in their ordinances providing for compensation when zoning is detrimentally amended.

The provisions relating to compensation in the four provinces are broadly similar (52). In each province the list of matters excluded from compensation is formidable (53). In fact in order to avoid the payment of compensation no Town Planning scheme has been approved in the Cape Province (54). Floyd comments on this circumstance in the following words: "The keeping of a scheme in the interim

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- (52) Kantorowich writes: "I think I should be correct in saying that the law as it stands at present permits a local authority to revise its scheme, provided that it again follows the procedure laid down for the preparation of the primary Scheme, but also provided that it compensates all owners for any loss which would be sustained, or abortive expenditure which would have been incurred, by virtue of removing or reducing any town planning rights (whether exercised or not) which the primary scheme had granted" ("The Problem of Re-development of Central Areas in Rapidly Expanding Communities", delivered at a conference of the Commission for Technical Co-operation in Africa South of the Sahara, in January 1959, at page 13). The circumstance referred to by Cooper in the following words seems a rather shocking exception to this rule: "In the Hercules Scheme near Pretoria the Townships Board on the advice of its technical advisers reduced the business area by quite 30 per cent - it merely instructed the local authority to amend map No. 3 in accordance with its wishes. No compensation has been paid and a few long faces resulted" (see "Proceedings of the Summer School of the South African Institute of Town Planners 1959", at page 35).
- (53) See Cape Townships Ordinance No. 33 of 1934, Sections 48 and 49; Natal Ordinance No. 27 of 1949, Sections 60, 61 and 64; Orange Free State Ordinance No. 20 of 1947, Section 46; and Ordinance 17 of 1952; Transvaal Ordinance No. 25 of 1965, Section 45.
- (54) Bouchier, "Comments on the Difference in the Town Planning Laws of the Provinces", "Proceedings of the Summer School of the South African Institute of Town Planners 1959", pages 20 and 22. See also Kantorowich: "The Development Charge Experiment in the Cape Province of South Africa", Journal of the Town Planning Institute, September/October 1964, page 348. The only compensation scheme to have been approved in Natal is that for Umgeni North. In terms of an amendment to the Durban "Town Planning Scheme in course of preparation" extensive rezoning has taken place in the Berea area without the payment of compensation.

stages for many years ... is most unjust and constitutes bad administration" (55). Floyd also states that the Cape Ordinance differs from those in other provinces and criticises it for not upholding the principle that zoning should not hamper existing uses by not allowing rebuilding or expansion and in this manner trying to 'freeze them out' (56). With respect to the United States, Ratcliff states that zoning is not retroactive and is not used to require the removal of non-conforming uses that exist at the time of the adoption of the zoning. Although one state in the U.S.A. has permitted retroactive zoning it is not generally thought to be constitutional (57).

(b) Betterment

Whilst there is nothing in South Africa comparable to the 1947 Act in Britain, Section 51 of the Transvaal Town Planning and Townships Ordinance (No. 25 of 1965) uses a system of development contribution based on a valuation before and after development. It is only applicable to amendments to an established scheme, and not to new schemes nor to community action. The development contribution is 50 per cent of the difference between the two appraisements. The amount is payable by the owner before any building plan is approved in respect of any new building or alteration where such plan would not be approved but for the scheme, or before the property is put to a use or purpose for which, but for the scheme or amendment, it could not have been used. It must be noted that there is no attempt, as there was in Britain in 1947, to place all properties on an equal footing. There is no question of purchasing the value of the development potential of every property and subsequently selling it

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(55) Op. cit. page 57. For a discussion of the treatment of non-conforming uses in South Africa see Floyd "More about Town Planning in South Africa", Chapter VII.

(56) Op. cit. page 179.

(57) "Urban Land Economics", page 413.

back to those owners who wish to exploit it. It is merely a matter of luck as to whether a particular property at present enjoys the right to develop in terms of its zoning or not. If it does the development charge is not applicable, and if it does not the charge must be paid. The fact that a property may immediately before the promulgation of the Ordinance have more than existing use value (because there is a demand for a more profitable use and the prospect that re-zoning would have been granted) is not allowed for in any way. Thus the question of whether betterment is payable is based upon the somewhat arbitrary criterion of what zoning the property at present has and not, as in Britain in 1947, what potential for redevelopment it possesses. The charge will also be arbitrary to a degree because there will be room for legitimate disagreement on the figures to be placed upon the value of the property before an amendment to the scheme and its value after the amendment. As implied above, one problem in valuation will be that where properties have had a potential for re-zoning because it was anticipated that they would be re-zoned, the prices at which they have sold will reflect not merely their value in terms of the existing zoning but some increment on this, allowing for the prospect that town planning permission would be granted to use the property for a more profitable purpose. Because land will have changed hands at a level above its existing zoning value and below its re-zoned value, the records of actual transactions may well be misleading. As the writer has already stated, the economic basis of a charge such as that embodied in the Ordinance is unsound (58). As the charge payable is only 50 per cent as compared to 100 per cent under the 1947 Act, the adverse effect of the Ordinance on the workings of the development market should not be as severe as was the case in Britain, but there is no doubt that the hazards of development will be increased and the development process retarded. In the Cape, Section 50 of the Township Ordinance (No. 33 of 1934 as amended) provides that where by

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(58) Supra, pages 112-117.

the coming into operation of any scheme or by the execution of any work a property is increased in value, the local authority may recover 50 per cent of the amount of the increase. No reference is made to the manner of collecting betterment. It should be noted that in fact betterment has never been claimed in the Cape (59). The Natal Ordinance No. 27 of 1949 has similar provisions for betterment to those contained in the Cape Ordinance, the maximum percentage claimable being 75 per cent. The Orange Free State Ordinance No. 20 of 1947 has no betterment provisions.

A concept, somewhat inappropriately called 'endowment', which all four provinces in South Africa embody in their ordinances has, to the writer's knowledge, no exact parallel elsewhere apart from Rhodesia. In terms of Section 14 of the Cape Townships Ordinance, the Administrator may require an owner wishing to subdivide land to pay an endowment "having due regard to community needs and public expenditure which he considers may arise from the establishment of such townships ... and the expenditure which has in the past been incurred and which in his opinion directly or indirectly facilitated the establishment of such township" (60). In practice the discretion of the Administrator in respect of the amount of the endowment demanded, whether in land or money, appears to be unfettered (61). Section 16 of the Natal Ordinance gives to the Townships Board of

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(59) Apart from an unsuccessful development charge experiment (see footnote (62) below), and under the Community Development Act, 1966 (see Chapter IV page 93 et seq. above).

(60) Kantorowich explains the purpose of an endowment to be to secure a local authority "against unforeseen future expense related to the particular development". See "The Development Charge Experiment in the Cape Province of South Africa", *ibid*, page 347. Unless an attempt is made to estimate expenditure it is difficult to understand the basis of calculation of an endowment charge. Nor can there be any assurance that the local authority will have reasonable security.

(61) See *Administrator, Cape Province v. Ruyteplaats Estates* 1952 (1) S.A. 541 (A.D.).

that province similar powers. In the Orange Free State the Ordinance makes no provision for payment of a money endowment in lieu of reservation of land, but in practice this distinction does not seem to be of consequence because an owner can be required to pay a sum of money to be fixed by the Administrator. Section 62 of Ordinance 25 of 1965 in the Transvaal provides for the Administrator to impose any condition which he may deem expedient including a provision of endowment whether in cash or in kind or both. The unsatisfactory nature of the provisions of these four ordinances in the light of the principles that have been discussed above is evident (62).

The only comparable concept in South Africa to special assessments (63) (apart from certain provisions for road construction costs) is that of 'special rates' which are provided for in the Cape Divisional Council Ordinance No. 15 of 1952 and the Cape Municipal Ordinance No. 19 of 1951. The special rate in the Cape is applicable to a portion of the Municipal area for the purpose of defraying the cost of any work, undertaking or improvement which in the opinion of the Council is for the special benefit of such portion. In the other provinces there is at present no general power to levy a special rate apart from Section 152 of the Transvaal Local Government Ordinance No. 17 of 1939 (as amended) for water and electricity undertakings and Section 50 of Transvaal Ordinance No. 25 of 1965 which provides that where expenditure is incurred by a local authority in connection with a town planning scheme, including any payment of compensation or under the urban renewal provision (Section 53) then that expenditure may be met inter alia by special rates. It should be noted that

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(62) For a discussion of a now abandoned experiment in the Cape Province in levying a development charge on urban property, see Kantorowich, "Town Planning in South Africa", Journal of the Town Planning Institute, March 1962, page 56, and Kantorowich, "The Development Charge Experiment in the Cape Province of South Africa", *ibid* at page 345.

(63) See pages 102-103 above.

special rates are concerned with recouping expenditure and make no reference to increases in the value of land in the area in which the work is done.

APPENDIX A

THE LAND COMMISSION ACT 1967 IN BRITAIN (64)

The British Government issued a White Paper in 1965 outlining the proposals which became embodied in the Land Commission Act 1967.

The principal objectives of policy set out in this paper were:

- "1. To secure that the right land is available at the right time for the implementation of national, regional and local plans;
2. To secure that a substantial part of the development value raised by the community returns to the community and that the burden of the cost of land for essential purposes is reduced."

These two objectives were to be achieved by the establishment of a Land Commission with wide powers to expropriate and by a betterment levy which was to be collected by the Land Commission. The levy was to be initially at a rate of 40% but with the intention of increases to 45% and then 50%, and possibly with further increases in future. Subject to certain qualifications, the Act gives the Commission the power to acquire land which it considers "suitable for material development". The Commission has the right to override servitudes and other rights over land which it acquires and to redispense of such land to developers clear of such obstructions. The Commission has the right to dispose of land for the best con-

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- (64) For detailed discussion of this Act, see Pennance "Housing, Town Planning & Land Commission", Leach "A Series of Articles on Betterment Levy", Estates Gazette 11/2/67 to 22/4/67, and Heap: "The Land Commission Bill Explained", Chartered Surveyor, July 1966.

sideration which it can reasonably obtain by way of freehold, or leasehold, or through a form of tenure described as "crownhold" which will ensure that any future value arising from the prospect of development will accrue to the Commission and not to the holder of the crownhold interest. The Betterment Levy applies in respect of all transactions and not only those where the interest is acquired by the Commission. It is chargeable wherever development value in land is realised. Development value is taken to be realised if prescribed calculations reveal its presence wherever a "chargeable act" or event occurs. Six cases of chargeable acts or events are set out. The levy is payable when development value is realised by the person receiving this value. Normally this would be when a transaction in land takes place. The Act is somewhat similar in concept to Transvaal Ordinance No. 25 of 1965 in that the levy is chargeable on the difference between the market or realisation value of an interest and its base value, the base value being the higher of its current use value (plus certain allowances) or the price paid for the land when last sold. Should capital gains tax be applicable, provision is made in the Act to avoid a double charge (65).

The purpose of the Act is to secure the objectives set out in the White Paper of ensuring the availability of land supplies, returning to the community a substantial part of the development value supposedly created by the community and reducing the cost of public acquisition of land. There appears to be no particular reason for the Land Commission's having been established as the agency for betterment collection (66). On the merits of the attempt to secure

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 (65) In the event of capital gains tax being introduced in South Africa, equity would seem to demand an amendment to the Transvaal Ordinance to prevent a double charge being made.

(66) See Pennance op. cit. page 26. In the opinion of West, "The Future Pattern of Ownership and the Development of Property", Estates Gazette December 7, 1968, page 1095, the betterment levy powers of the Land Commission are almost certain to be transferred to the Inland Revenue in the near future whatever political party is in power.

the value for the community which is thought to have been created by the community and of reducing the cost of public acquisition of land, comment has already been made (67).

The principle of ensuring the availability of land supplies seems in part to set the Land Commission up as an urban renewal agency (68) but in part to go beyond this and to be based upon the assumption that land-owners are withholding large quantities of land for speculative purposes. The Commission's report for its first year ending in March 1968 indicates in fact that it found little in the way of land hoarded by private individuals waiting for a price rise (69). The short period of operation of the Act to date makes it impossible to reach any firm conclusions about its effectiveness but gives rise to little optimism. The Betterment Levy appears to be creating the same difficulties as those which arose in the 1947 Act and one is led to wonder whether the Land Commission Act will suffer the same fate. It seems probable that the supply of land coming on to the market is being deterred by uncertainty, by the reduction of the net rewards to the seller and by the political threat from the Conservative Party which has undertaken to repeal the Act at the earliest opportunity (70). The stated view of the Conservative Party is that profits from dealings in land are legitimate taxable sums, but if such profits were to be taxed it should be done through the normal taxation administration (71).

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(67) See respectively "An Attempt to State a General Principle" at page 112 et seq. above and Chapter III "Cost-Benefit Analysis" at page 63 et seq. above.

(68) See discussion of Urban Renewal above, Chapter III at pages 50-63.

(69) See "The Commission's First Year" leading article in the Estates Gazette of October 19, 1968.

(70) See Pennance op. cit. at pages 41 and 50.

(71) Estates Gazette, February 15, 1969, page 707.

CHAPTER VI

RATES

PART 1 - GENERAL CONSIDERATIONS

INTRODUCTION

This chapter does not set out primarily to examine the efficacy of rating as a means of raising revenue; it is concerned principally with the equity of rating as a form of taxation and, whether or not rating be accepted as equitable, with the methods of application of rating which will result in the least inequity and at the same time create the minimum economic distortion.

RATING AND THE CRITERIA OF SOUND TAXATION

In so far as taxes are imposed merely to raise revenue and without wider political objectives, it would probably be generally agreed that the following are the more important criteria of a sound tax (1):

- (a) There should be a definite relation between the ability of a person to bear a tax and the amount of the tax imposed upon him.
- (b) The tax should have a definite relation to the benefits received.
- (c) The yield should be reliable.
- (d) The tax should be economical to administer.
- (e) The tax should have the minimum effect upon the workings of the price mechanism, i.e. should disturb the optimum allocation of

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- (1) No priority is implicit in the order in which these criteria are listed.

resources to the least possible extent.

(f) The tax should be socially expedient.

We proceed to consider whether rating is a sound tax in the light of the above criteria.

(a) Ability to bear

Rating as a form of taxation had its origin in countries of British settlement in the Elizabethan poor rate, if not earlier. At that time there was a close relationship between the amount of landed property a man held and his ability to bear tax. With the development of modern industrial society there has ceased to be any real relationship between the ability to bear tax and landed property ownership. The effect of rating as a form of taxation today is that in terms of ability to bear some escape almost entirely and others pay greatly excessive taxes. Moreover, the systems of rates assessment are usually such that the tax imposed is not even equitably related to the income produced by a property. The British system whereby rates are levied on annual and not capital value is, at least in principle, an exception (2). It should be noted that in the absence of State interference with the price mechanism, rating taxation tends to be regressive because the poor usually spend a higher percentage of their incomes on housing than do the rich (3).

(b) Benefits received

Rating taxation is more closely related to benefits received than income tax in consequence of its local nature and because, lacking

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(2) For a general discussion of rating practice in Britain, see Bean and Lockwood, "Rating Valuation Practice", 5th Edition, or Eve, White and Wilks, "Principles and Practice of Rating Valuation", 2nd Edition.

(3) For discussion of the shifting of rates from landlords to tenants, see below, page 138.

any progressive element (4), it causes less re-allocation of wealth. To at least some extent the expenditure of property taxation on fire protection, roads and the like counterbalances the cost of the tax to the owner of property. However, there is no necessary relationship between the tax any individual pays and the benefits he receives.

Onerous rates are those which do not confer a net benefit on the ratepayer; beneficial or remunerative rates are those spent on roads, drainage and the like which result in a net benefit to the ratepayer (5). A particular rate may be onerous for some ratepayers, but remunerative for others. Hoyt's analysis of rating showed that in general commercial and industrial properties and higher priced houses yielded a surplus to the local authority, while medium and low priced houses cost more than they yielded (6).

There is a marked trend in South Africa and elsewhere for more and more rates income to be spent on public health, social welfare, traffic control and like activities (7) and for a decreasing proportion of expenditure to be in respect of roads and other services which tend to increase site values. Consequently with the passing of time rating taxation is becoming less and less related to the benefits obtained by the property owner.

The annual value system as used in Britain where rates are imposed on the occupant and not the owner, as has been noted, accords better

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- (4) A progressive tax is taken to be one which rises more than proportionately with a rise in the capital value or income upon which the tax is imposed.
- (5) Marshall, "Principles of Economics", 8th Edition, page 655. See also Thompson "A Preface to Urban Economics", page 307.
- (6) Weimer and Hoyt, "Principles of Real Estate", 4th Edition, page 457. This circumstance tends to offset to some extent the regressive nature of rating as a form of taxation.
- (7) In particular non-European requirements are becoming an increasing burden upon the ratepayer.

with the ability to bear principle than does the capital value system; similarly, when rates are spread over a large body of tenants, rather than imposed on a smaller number of owners, there is likely to be closer accord with the benefit received principle (8).

Local rates also result in benefits being received by persons who have made no contribution to local expenditure because it is frequently the case that no rates are paid by those who live beyond the boundaries of a local authority. The residents of extra-urban areas make frequent use of the transport, cultural and other facilities of the town without making any contribution (at least via rates) to their cost.

(c) Reliability

While it is true that the yield from property tax is stable, this is a doubtful advantage in an inflationary age. The costs of assessment are such that revaluations are feasible only at intervals of several years. Further, with fluctuations in the economy the burden of rates may fall hardest upon the taxpayer when he is least able to meet them. Systems of rating based on annual or rental value are more responsive to economic fluctuations than systems based on capital value because the capital value of property tends to fluctuate less than rents. In periods of depression the liability for rates will decrease, whilst in boom periods it will rise. On the other hand, from the view-point of the local authority the rate income under a capital value system has the advantage of being more stable. Moreover, property taxes are seldom avoided or evaded.

(d) Economical administration

It is sometimes asserted that because real estate cannot be concealed, rates are an economical form of collection. In the light of the high cost of any value assessment which does not proceed upon

- (8) Although under a capital value system the burden may be shifted to tenants. (See below, page 138.)

arbitrary principles, this is doubtful. Some observers have concluded that the problems of valuation are so severe as to leave no alternative to the abandonment of rating as a system of local taxation (9).

(e) Minimum distortion

That property taxation adversely affects the optimum allocation of resources is certain because it has the inevitable effect of arbitrarily diverting capital into other forms of investment by reducing the return available from property. As landed property ownership has ceased to be indicative of wealth, there is little justification for its being singled out for a special form of taxation, except in so far as the expenditure of rates is beneficial to property owners.

(f) Social expediency

The explanation for the almost universal continued use of rating is that the public has been conditioned to its acceptance for generations and thus raises little protest, that its abolition would lead to unearned increments in the value of landed property (10), and that it has some merit of a political, if not an economic character in that it encourages local independence and thus provides a foundation for democratic responsibility.

SITE VALUE RATING

The land taxation theory to which Henry George (11) gave form in the latter part of the nineteenth century requires to be discussed because

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- (9) See Cowden, "The Valuation of Property for Rating Purposes", a paper presented to the Institute of Municipal Treasurers and Accountants of South Africa in March 1948, page 226.
- (10) For a discussion of the "capitalization of rates", see below, page 138.
- (11) "Progress and Poverty". For a discussion of the influence of Henry George in the field of Town Planning, see Chapter V, pages 112 and 117.

it would appear to have some influence in South Africa. The theory is based upon the view that land value derives from communal causes and not the efforts of any individual, that the benefits from it should belong to the community and that the entire income derived from land (but not from improvements thereon) should therefore be taken in taxation.

Economic rent can be defined as the surplus of income over the minimum supply price required to bring a factor into production. According to the 'pure' theory of rent, land has no cost of production and its value is capitalised economic rent. Thus it is held that a tax on land will not reduce supply but simply the return to the owner (12).

The pure theory of rent has little practical application because of the differences between its assumptions and the conditions of the market place. Land and buildings are inextricably linked together and it is hardly possible to distinguish their respective contributions. Henry George, moreover, appears to have overlooked the contribution of those who maintain and improve land, and to have assumed that the prospective use of a site would be unaffected if the anticipation of income from the site were removed (i.e. that all income derived from a site was necessarily economic rent). Further, there is no method of establishing what part of the value of a site derives from community action and what from the skill and enterprise of present and past owners. Value is an amalgam of both (13).

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(12) However, even if the tenets of the pure theory are accepted, a change to land taxation will not be without economic consequence. The introduction of a tax on land values may compel the discontinuation of marginal operations where the rates burden rises, and will generally lead to some change in the pattern of land usages.

(13) P.H. Clarke "Site Value Rating and the Recovery of Betterment" in "Land Values" at page 86 writes: "Enhancement in land value is generally the result of public policy, action or influence in one or more of its various forms, but, nevertheless, it is also true that some small part of the enhancement may be due to the activity or enterprise of the owner". In the writer's view Clarke does not comprehend the operation of the market and the collective impact of the action of owners.

Whenever an entrepreneur successfully pioneers a location his risk-taking produces an enhanced land value. Apart from the improvements on a particular piece of land, its economic value is determined not only by its natural qualities but by improvements in its environs, such as drains, roads, shopping centres and other agglomerations of favourable land uses, public transport, electricity and water, which may well in one way or another have been paid for by those who have held the ownership of the land.

It is only in an abstract sense that the rent from land can be regarded as unearned. Urban land economics today is based on the equilibrium explanation of price and does not require to distinguish between factors of production which are determined by price and those which determine price. Whilst land may be fixed in a physical sense, it is economically mobile in that it moves towards the usage which will produce the highest returns (14). The rent from land is in fact based on opportunity cost, i.e. the returns which can be obtained from alternative uses (15).

Rating on land value only accords even less with the basic criterion that people should be taxed according to their ability to bear than does rating on both land and buildings (16). There is no necessary

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(14) Subject to such limitations as may be imposed by town planning.

(15) See Ratcliff, "Urban Land Economics", page 367. Pennance "Housing, Town Planning and the Land Commission" at page 42 writes: "This argument (i.e. the pure theory of rent) refers to a fixed stock of land. But land for development is not a fixed quantity. Like the supply of any other commodity, more land will be forthcoming the higher the price offered, and conversely. In deciding whether or not to market land, owners will weigh developers' bid prices against their own preferences for sites or the values realised for their existing uses. It follows that a tax on development value in land will reduce the quantity forthcoming at any given price and/or raise the price level at which a given quantity would be made available to the market."

(16) See Horwood, "Local Government Finance in South Africa", South African Treasurer, August 1966, page 144.

relationship between the ratio of land value to building value of any property and the ability of its owner or occupant to bear rates, and frequently property owned or occupied by the poor has a higher land value ratio than property owned or occupied by the rich. Under site rating, rates fall relatively more heavily on owners with smaller buildings per unit area of land than under flat rating (in terms of which an equal levy is imposed on land and buildings). In areas where commercial usage is replacing residential, a large office building may pay the same rates as an adjoining house. A change to site rating might force house owners in such an area to spend a considerably higher proportion of their income on housing, or to sell at a capital loss. An effect of land taxation is in fact to force more intensive land use (17). This can have the injurious result of driving development beyond the optimum degree of intensity with resulting misallocation of resources through premature or otherwise inappropriate land usages.

It is argued in favour of land value taxation that it reduces the prices of undeveloped sites, but this is not necessarily true. The rates payable on a newly developed site may well be lower (and land value higher) under a system of land rating only than when both land and buildings are rated. If the ratio of site value to total value of the ratepayer's property equals the average ratio within the rating authority's area, the same annual amount of rates will be payable irrespective of how the rate is levied. If the ratio of site value to total value is less than the average, the ratepayer will pay a decreasing amount in rates as the levy on buildings is decreased, i.e. as the system of rating employed moves towards site rating only. Domestic property will in general benefit by a change from flat rating to site rating because single dwellings generally have a site to total value ratio which is less than the average for

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- (17) It is paradoxical that the effect of development charges which commonly have their roots in the same philosophy as does site rating, is precisely the opposite, viz. to discourage development. See Chapter V above, pages 104-105.

all types of property in a town. In general, the assertion that site rating will lower the prices at which fringe land is sold is not true (18). Site value rating tends to discourage building on the fringe of towns and to cause greater concentration because switching rates from buildings to land causes developers to use less land and increase investment in buildings. A switch to site rating would tend to raise the value of expensive buildings and new buildings and lower the value of cheaper buildings and older buildings (19). New buildings will tend under a site rating system as compared with a flat rating system to be built relatively sooner and to be relatively more expensive.

Land value taxation is further advocated because it discourages speculation. Whilst this may well be so, speculation is not necessarily (or indeed normally) undesirable because the person who holds land for future development may well render a service to the community by foreseeing a ripening usage. Moreover, the compound loss of interest on idle land is almost always a much weightier factor than the payment of rates. Similarly, the claim that site rating increases the turnover of properties is of doubtful validity in practice and it is in any event difficult to understand why increased turnover as such should be socially desirable. But an undoubted tendency of land value rating is to tax open spaces out of existence.

The land tax theory disregards the risks which attach to land and overlooks the fact that the capitalisation rate at which the present purchase price of a property is calculated allows for the prospect of future increases in value. If the theory were ever fully applied (i.e. if the entire income from land were taken in taxation) it would destroy the process of allocation of land resources together with any incentive for the enhancement of land values through entrepreneurial

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(18) See Turvey, "The Economics of Real Property", page 91.

(19) See Marshall, op. cit., page 659.

action (20).

The philosophy of the single tax theory may be contrasted with the fact that the expenses of local government probably grow more in proportion to real estate development than to rises in land values, which might suggest that rates should be levied on improvements only (21).

POTENTIAL VALUE v. REBUS SIC STANTIBUS

Rates based on capital value (and most markedly rates imposed on site value only) conflict with the principle of rebus sic stantibus, namely that for rating purposes property should be valued in the usage and other circumstances existing at the time of valuation (22). Rates assessed on capital value are a tax on potential rather than actual use and a tax therefore which has to be paid on the assessor's speculations about the future. The British system based on annual or rental value is the most equitable form of rating because it corresponds most closely to the ability-to-bear criterion (23). Moreover, except in the case of single dwellings, the process of assessing annual value will generally be less complex than the estimation of capital value (unless entirely arbitrary processes are adopted to find a capital figure (24)).

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(20) For a discussion of the effect of the Town and Country Planning Act of 1947 in Britain, see Chapter V pages 104-105.

(21) See Bonbright, "Valuation of Real Property", page 509.

(22) For a discussion of the interpretation of this principle in English Case Law, see Bean and Lockwood, op. cit., page 14.

(23) In respect of property where there is no demand other than the existing use it will be indifferent whether the rating system is based on potential value or existing use value.

(24) For a discussion of the difficulty of estimating the capital value of a property which is likely to be subject to a change of zoning, see Chapter IV page 85.

A potential value system of rating departs from normal taxation practice in that in effect it levies tax on the income a taxpayer ought to earn as compared with that which he does in fact earn (25).

Against the objection raised that unused land pays no rates under an existing use value system (at least as previously applied in Britain) must be set the fact that the local authority renders little or no service to such land (26).

The valuation of land under a potential use system is to a material extent dependent upon the usage permitted under the town planning scheme. Thus the town planner will effectively dictate the amount of rates the owner pays (27). Potential use rating has the result of imposing an annual development levy because of the possibility.

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(25) See Ward, "The Taxation of Land Values in the Transvaal by Local Authorities", South African Journal of Economics, March 1942, page 16.

(26) It is to be observed that an undertaking of the local authority may increase the capital value of unused land. In so far as the expenditure by the local authority is constituted by the provision of proper services for which the developer of land could reasonably have been made responsible, it is practicable and justifiable to levy charges on the owners of pieces of land at such time as the services come to be utilised; to the extent that expenditure by the local authority cannot be attributed to services immediately related to a particular piece of land it will not be practicable to levy a charge and the cost will be borne by the general body of ratepayers. See Chapter V page 117. In the latter circumstances the owner of unused land may obtain a benefit under an annual value system at the expense of ratepayers. To the writer's mind the exemption from rates of unoccupied property is not an essential feature of a rating system based upon existing use and it would be compatible with such a system for unoccupied property to be rated at the most profitable use to which the property in its existing state of development could be put within a reasonable period of time.

(27) See "Rating of Site Values - Report on a Private Survey at Whitstable" published by the Rating and Valuation Association, page 12 (abridged edition). In order for land to have a potential use above its existing use there must of course be demand for the more intensive use permitted by the planning scheme.

that there may in the future be a change in usage (28).

THE INCIDENCE OF RATES

It does not necessarily follow that the economic burden of a tax will fall upon the person legally responsible for its payment. Rates, at least in so far as they fall upon buildings, tend to be shifted over a period by landlords to tenants because, except where the demand for accommodation is elastic, an increase in the rates payable by the landlord will lead to higher rents through the withholding of capital from development creating a relative decline in the supply of accommodation. Rates levied on the owners or occupiers of residential accommodation will remain with the occupier, but rates on commercial and industrial property are part of the costs of production and can sometimes be shifted, at least in part, to customers (and less frequently to suppliers and employees). To the extent that an increase in rates cannot be shifted the burden of all future payments will remain with the present owners of the property even after its sale because the purchase price of a property is a function of its anticipated net income and the purchaser will consequently deduct the capitalised value of future rates from the price he would otherwise pay.

The industrialist's ability to shift an increase in rates will depend on the universality of the tax and his control of the market. When his product is sold nationally in a competitive market and the rise in rates is local the full burden is likely to remain with him. Producers with price setting powers (those in a monopolistic or semi-monopolistic position) who have adjusted their prices to produce the

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- (28) The development levy now imposed in the Transvaal under sec. 51 of Ordinance 25 of 1965 seems hardly equitable when account is taken of the annual levies that have in effect been imposed through the employment of a potential value system. See discussion by G.H. Halliday, "Imposts on Land and their Effects on Land Development", unpublished thesis M. Econ, University of Natal 1963.

maximum profit will have to bear at least part of the increased tax (29). The ability of landlords to shift rates to tenants depends upon leases and market conditions. The assertion of Jordan that all economists agree that the burden of rates on business property is in the long run shifted is hardly correct (30). Nor is it in fact "fair to assume that within a year or so some fairly substantial portion of the increased burden will have been passed to the consumer" (31). There is probably general agreement that to the extent that tax is levied on the site, it cannot be shifted (32). Because of the lengthy period over which buildings are consumed the transfer of an increase of rates is much slower than would be the case if they were imposed on more rapidly consumed commodities. The suggestion of Haygarth that "in so far as flat dwellers are concerned there should not be any difficulty in an owner passing on the burden of an additional taxation direct to such flat dwellers" is also too facile (33).

In practice it is probable that the conditions where the entire burden can be shifted will exist only in a minority of cases. The typical case will be that only part of the increase will be shifted

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(29) See Barlowe, "Land Resource Economics", page 542.

(30) Jordan, "The Durban Rating Story", South African Treasurer, September 1965, page 131. A similar statement is made by Haygarth, "Differential Rating", a paper presented to the Institute of Municipal Treasurers and Accountants of South Africa in April 1964 at page 270: "It could be said generally that in so far as the commercial and distributive field is concerned all owners in the area would be affected and would likely pass the whole burden to the consumer except to the extent that the demand was extremely elastic".

(31) Jordan, loc. cit.

(32) Barlowe, op. cit., page 541; Chambers, "Some Aspects of Local Government Taxation in South Africa", a paper presented to the Institute of Municipal Treasurers and Accountants of South Africa in March 1951, page 262. For the difficulty of distinguishing rates falling on land and on buildings, see above page 132.

(33) Op. cit., page 240.

and that some decline in property values will occur (34). As the home-owner is not in any way able to shift the burden of rates, the greater the proportion of single dwellings in an area, the greater the proportion of rating expenditure that will come directly from its inhabitants (35).

WHAT VALUE?

The question arises whether rating assessments should be based on 'value to the owner', 'market value', or some arbitrary formula (36). Bonbright suggests that whilst 'value to the owner' can never be a satisfactory test, it is more equitable than 'market value' (37). However, because of the inapplicability of the ability-to-pay criterion in rating taxation and the grave practical difficulties in estimating 'value to the owner', it seems to the present writer that market value is the best basis. Bouchier (38) objects that under the market value test the man who builds a mansion which has a market value less than its cost will pay rates on less than his outlay on his property. However, if the man who built the house sells it, the purchaser will only pay market value and there can be no justification for asking him to pay rates on a capital sum in excess of his purchase price. In the writer's opinion the only arguments in favour of arbitrary formulae employing the summation method of valuation which have any justification are those based on grounds of economical administration and not of equity (39).

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 (34) See generally McCrystal, "A Problem of Rating in the Case of Durban", South African Journal of Economics, Sept. 1963, p. 212.

(35) Lichfield, "The Economics of Planned Development", page 157.

(36) For definitions of the concepts "value to the owner" and "market value", see Chapter II pages 6-7 and 11.

(37) Op. cit., page 458.

(38) "Valuation in the Cape Province", South African Survey Journal, December 1962, page 11.

(39) For a discussion of the summation method and the impossibility of estimating depreciation other than by first finding market value and then deducting replacement cost, see Chapter II pages 10-11.

It would seem that if the inequities of rating as a system of taxation are to be minimised all properties should be valued at market value or at an identical proportion of market value. Further, the value to be taken is market value in existing use, not market value in potential use (40).

It is a criticism of rating valuations both in the United States and in South Africa that rating assessments do not accurately reflect market value. The expense of employing personnel qualified to undertake scientific valuations is so considerable that men with inferior training are currently employed by public authorities (41). Hence it is inevitable that the rates on some properties will be high in relation to market value and on others low. Where rating assessments are made on an arbitrary basis this should be publicly recognised in order that they should not be used as a basis of valuation in such fields as rent control, expropriation, insurance and investment (42).

FLAT, COMPOSITE, SITE AND DIFFERENTIAL RATING

A flat rating system imposes an equal levy on land and buildings, and a site rating system levies rates on land only. The terms 'composite rating' and 'differential rating' are frequently confused. A composite rating system is one which adopts an intermediate position between flat and site rating (the levy on the site value being higher than on the building value), whereas a differential system

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(40) See discussion above headed "Potential Value v. Rebus Sic Stantibus".

(41) At least part reason for the abandonment of the 1968 quinquennial rating revaluation in Britain has been the difficulty of obtaining suitably qualified personnel. See footnote 50 below and Estates Gazette, October 19, 1968, page 293.

(42) For comment on the use of rating assessments in estimating compensation upon expropriation, see Chapter IV pages 83 and 93; for comment on their use in establishing controlled rents, see Chapter VIII page 194.

is one which is deliberately discriminatory through imposing a higher levy in the rand on certain types of property or through the exemption of certain other types of property. The recent controversy about rating in Durban turned upon the desire of the local authority to discriminate against certain types of property (43). The motive behind the selection of a site rating or a composite rating system can also be the wish to discriminate against certain types of property because, as has been shown (44), the ratio of land to total value tends to vary with different types of property.

EQUITY AND RATING AS BETWEEN DIFFERENT TYPES OF PROPERTY

If the principle were accepted that the burden of taxation should be shouldered only by the ultimate consumer (as would appear to be the premise of income tax in countries where no company tax is levied) on the grounds that this would cause the minimum distortion in the economy or that it was thought to be equitable, then property used for productive purposes would not be rated. The contrary view holds that productively used property should carry a heavier tax burden than purely residential property (45). This view was the basis of the differential rating system proposed by the Durban Municipality. Haygarth goes so far as to state that to the extent that the inclusion in rateable value of stock in trade and plant and machinery would outweigh the inclusion of movable property in the case of home owners, the distribution of the tax burden is inequitable as between the domestic and business sector (46). Jordan holds that

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(43) See McCrystal, loc. cit., Horwood, loc. cit., and Jordan, loc. cit. In terms of Section 107 of Ordinance 21 of 1942 as amended by Section 8 of Ordinance 27 of 1966, municipalities throughout Natal have obtained the power to discriminate against non-residential property.

(44) See above, page 134.

(45) See McCrystal, op. cit., page 209.

(46) Op. cit., page 215.

there can be no meaningful discussion of equity in rating as between business and residential properties and concludes that it is indifferent as to how rates are levied on business and residential property (47). Thus in Jordan's view there is no argument in equity to prevent a local authority from doing whatever it pleases. Marshall, on the contrary, suggests that it may be equitable to rate business property only in so far as the rate can be shifted (48). It seems to the present writer that there can be no certainty about how a tax will be shifted, that it would be impracticable for rates to be levied on non-productive property only (apart from other considerations the de-rating of productive property would cause an unearned accretion in its value), that there can be no final conclusion to the debate on equity and rating, and that the least arbitrary course is to impose a level rate on all forms of property.

CONCLUSION

Seligman (49) writes that rating is "beyond all doubt one of the worst taxes known to the civilised world". Bonbright is of the opinion that the system of rating in the United States has no 'valid philosophy' and that a reform of the whole system is needed (50).

Various alternatives to rating suggested from time to time have been:

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- (47) Op. cit., pages 180-182.
 - (48) Op. cit., page 661.
 - (49) "Essays on Taxation", quoted by Cowden, op. cit., page 173.
 - (50) Op. cit., page 508. The South African Treasurer of May 1966 page 104, is hardly correct in stating that no reformer has suggested the abolition of rating. In Britain the government has announced its intention to abolish rating and introduced a reformed system of local taxation. No indication has been given as to when the firm proposals will be announced or what form they will take. However, the quinquennial rating revaluation due in 1968 was abandoned. (Chartered Surveyor, January 1966.) In some countries on the European continent rating is not employed and additions are made to State taxes for local purposes. See Cowden, op. cit., page 179.

central government grants in lieu of rates, motor vehicles and petrol taxation, profits from public utilities, sales taxes, taxes on employed persons and local income taxes (51). In the opinion of the writer the evils of rating are outweighed by the autonomy that it vests in local government. In order to minimise the detrimental effects of the system the following principles should be observed:

(a) The system should be employed only in circumstances where rates are beneficial for property owners (or tenants) as a whole (52). Revenue for other local purposes (53) should be raised by other means. There is otherwise no justification for singling out real estate as a basis for taxation (54).

(b) For purposes of rating all properties should be assessed at market value in existing use and not at market value in potential use nor at value to the owner; arbitrary methods of assessment such as the summation procedure should not be employed.

(c) The flat system of rating should be employed exclusively.

(d) Ideally, a fair levy should be imposed upon extra-urban property which benefits from the facilities provided by a town. This, however, may be a counsel of perfection and the costs of making the

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(51) In South Africa rates as a percentage of total taxes have declined but in real terms have been remarkably constant per head of urban population and have also maintained a remarkable constancy in proportion to national income. See Horwood, op. cit., page 156.

(52) See above, page 129.

(53) There is a considerable variation between various countries in the services financed by local authorities. It is also often difficult to determine the extent to which a particular undertaking will be beneficial to property owners. The only test is one of remoteness and this by its nature cannot be exact.

(54) It is of interest that in the Cape Colony rate income was restricted to services of benefit to property. See South African Treasurer, October 1955, page 188. The Local Authorities Committee (the Borckenhagen Committee) has recognised that the ratepayer "cannot be expected to finance so many services not of benefit to his property". See South African Treasurer, August 1964, page 147.

attempt, together with the risks of introducing fresh unintended distortions, should occasion extreme caution.

Finally, it should be noted that any change in an existing system of rating should be made gradually because it will inevitably result in unearned losses and gains in the capital value of properties.

PART 2 - THE SOUTH AFRICAN POSITION

Rating legislation in South Africa is a matter within the control of the provincial councils and not of Parliament (55). Rates are an impost on urban (and peri-urban) property but not (except in the Cape Province) on rural land (56). Capital and not annual value systems are used in all towns. Throughout the country rates are imposed on landlords and not tenants. All systems are based upon potential and not existing use (57).

In all provinces the assessor is instructed to estimate the market value of land. The value of buildings in the Transvaal is correctly taken to be the difference between the market value of the improved

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(55) For the historical development of rating in South Africa, see Cowden, loc. cit.

(56) In the Cape Province all land is taxed in terms of the Divisional Councils Ordinance 26 of 1944 (C) (as amended). This includes the areas of municipalities which in addition have separate rating power under Municipal Ordinance 19/1951 (C). Rating powers in other provinces embrace only towns and other defined areas. In the Transvaal, Natal and the Orange Free State rating powers were provided respectively by the following ordinances: Local Authorities Rating Ordinance 20/1933 (T) and Peri-Urban Health Board Ordinance 20/1943 (T); Local Government Ordinance 21/1942 (N) and Local Health Commission (Public Areas Health Control) Ordinance 20/1941 (N); Local Government Ordinance 8/1962 (O) and Smallholdings Ordinance 17/1954 (O). See Halliday, op. cit., page 31.

(57) See discussion of decision in *Geldenhuy's v. Johannesburg Municipality* 1917 TPD.241 in Chapter VII below at page 159.

property and the market value of the site, but in Natal, the Cape and the Orange Free State, buildings are taxed on their replacement cost less an arbitrary figure for depreciation.

Within certain limits, municipalities have discretion in the allocation of rates as between land and buildings. There are marked differences in the practices in various provinces. In the Cape flat rating predominates (58); the Free State employs both flat and composite rating; in Natal composite rating is used; the Transvaal is *the stronghold of site rating*. The theory of Henry George would appear to have had more than a little influence because, of the larger municipalities, only Cape Town and Port Elizabeth charge an equal percentage rate on land and buildings. Johannesburg and other Reef municipalities, with the exception of Germiston, do not levy any rates on improvements. The other major towns in the country have adopted an intermediate position. Differential rating has only been employed in limited and special circumstances (e.g. where normal municipal services have not been extended to a particular area (59)).

A comparison of the level of rates in different South African towns is somewhat difficult. This is partly because of differences in the methods of valuation and the varying levies on land values and building values. The position is complicated by different degrees of under-valuation (and occasionally over-valuation) in various towns and by the lack of uniformity in the services provided to the rate-payers. For example, where flat rating is employed it is usual for sewerage and sanitary removal to be included in the general rates

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(58) East London has been a battleground between the proponents of flat rating and site rating. The levy imposed has varied notoriously with resulting haphazard fluctuations in property values. See Chambers, "Rates and Ratios", South African Treasurer, September 1961, page 177.

(59) See Walker, "Rates and Rating"; South African Treasurer, April 1953, page 92; Reid, "Differential Rating", South African Treasurer, March 1959, page 74 et seq.; Horwood, op. cit., page 144. The recent change to the Durban rating system has no precedent in South Africa.

charge, but where site rating is used special rates are levied for such services.

Regrettably, in all provinces appeals to the Supreme Court from rating courts can be made only on points of law and the quality of assessment cannot be tested before the judiciary. As few judges can possess any knowledge of land economics, it would be desirable to establish a specialist division of the Supreme Court to hear rating, expropriation and like appeals (60). In the Cape Province rating assessments are conducted by the Provincial Administration but in other provinces they are made by the local authority. On this point there is urgent need for reform in the Transvaal, Natal and the Orange Free State; it is most undesirable that valuations for rating purposes, an essentially judicial function, should be conducted by a body immediately answerable to an electorate (61).

THE CAPE VALUATION ORDINANCE

Ordinance 26 of 1944 (C) in respect of land valuation lays down a set of directives to valuers and provides for a system of sample values which have to be employed when valuing supposedly 'similar' property. It is fortunate that the Cape is the only province in which this system is employed because in practice it has been found that it hinders the work of valuers and gives rise to anomalies. The three other provinces in not fettering the judgment of the valuer have shown a more realistic appreciation of the valuation

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(60) Under common law the Supreme Court has an inherent right to revise the decisions of administrative and quasi-judicial bodies but the benefit of this right is largely negated by the absence of any common law requirement that such bodies record the reasons for their findings. This circumstance is not conducive to justice and it is to be hoped will be remedied by statute. See Rose Innes, "Judicial Review of Administrative Tribunals in South Africa", Chapter 13.

(61) See Hicks, Hicks and Neser, "The Problems of Valuation for Rating", quoted by Cowden, op. cit., page 172.

process. In the year before the Cape Ordinance was promulgated R.L. Ward wrote an article which one can only think was never read by any member of the Cape Provincial Council (62). He exposed the foolishness of its basic conception in the matter of land valuation and attacked some of its more glaring absurdities (63).

Regrettably, whilst the Cape Provincial Council has tidied up the wording of its Ordinance, it has not rejected its basic concepts (64). The legislature continues to lay down an artificial basis of valuation despite the statement in clause 43(1) that land is to be valued at the ordinary price which it is estimated a buyer would be willing to give and a seller would be willing to accept if the land were brought to voluntary sale. It still requires the valuer to examine the records of properties kept by the local authority or by the magistrate (Section 43(2)) although any competent valuer would apply his mind to all property transactions of which reasonably reliable evidence could be obtained. It remains unnecessary to instruct the valuer that he is to consider whether any price was due to exceptional circumstances (Section 43(2)) because the competent valuer would not regard such a transaction as being evidence of value.

The essential absurdity of the ordinance in respect of land valuation is the conception embodied in Section 43(3) that from the

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- (62) "Note on Cape Town Draft Ordinance", South African Journal of Economics, 1943, page 72.
- (63) With justification, Ward said of one clause that it was "incomprehensible", of another that "the reader is completely at a loss to understand what can be meant" and of a third that "it almost indicates illiteracy". Yet these clauses stood on the Statute Book for sixteen years until, perhaps, some enlightened official browsed through a dusty bookshelf and stumbled upon Ward's strictures. Such slovenly draughtsmanship deserves to be so castigated because rating legislation has material social consequences.
- (64) In 1953 a report was published of a committee which had been appointed to investigate the assessment of property for rating purposes in the Cape. Fortunately, its whimsical proposals were ignored.

selection of "guides" the values of all other properties can be assessed. It is patent that no two pieces of land are wholly identical and that in a very short distance (in the centre of the city within a very few feet) the value of land can differ radically. In the assessment of land values it is necessary for property under examination to be compared with every other property that has been sold that is in some degree similar, and the writer is compelled to assume that in practice valuers in the Cape Province can pay little heed to the samples upon which they supposedly base their conclusions.

Clause 43(17) which lists an inevitably incomplete and wholly unnecessary variety of items that are to be taken into account, hardly flatters the valuers employed by the Cape Provincial Administration. A man who required to be told to consider such matters in valuing property would be wholly incompetent for the task.

Finally, some comment is required on the employment in the Cape, as in Natal and the Orange Free State, of the summation method of valuation (65). Section 44 reads: "The basis of valuation of buildings shall be the estimated cost of erection (66) at the time of valuation, less such allowances as may be considered due on account of structural depreciation, obsolescence or a change in the nature of the locality since the erection of the building concerned." According to Bouchier (67) 'depreciation' represents the amount by which a building has deteriorated in value purely through age or the type of construction, and 'obsolescence' represents the amount by which the value of the property has dropped through the fact

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(65) For a discussion of this method, see Chapter II pages 10-11 and Chapter IV pages 83-84; and for judicial comment, see *Pietermaritzburg Corporation v. S.A. Breweries Ltd.*, 1911 A.D.511 and *Durban Corporation v. Lincoln* 1940 A.D. 36.

(66) The meaning of the term "cost of erection" is considered in *Cuthbert and Co. Ltd. v. Director of Valuations* 1936 C.P.D.10.

(67) *Op. cit.*, page 11.

that it is no longer suitable for the purpose for which it was erected. The writer has difficulty in understanding the meaning of these words. It appears to him that depreciation is loss in value from whatever cause and that any attempt to allocate it will be ineffectual. There is no valid method by which depreciation can be estimated other than through assessing its present value and deducting therefrom the original cost of a property - an exercise of no obvious purpose. Further, if the method under the ordinance is to be employed, when a warehouse surviving from the days of Jan Compagnie is to be assessed for rating purposes, are we compelled to consider the present costs of building with boulders and mud and yellowwood, or shall we have regard to a reinforced concrete structure of similar floor areas (68)?

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(68) See discussion in Chapter II above under heading "Replacement Cost Approach" at pages 10-11.

CHAPTER VII

THE VALUATION OF LAND FOR SUBDIVISION

This chapter is divided into two parts: the first states the economic principles applicable in valuing land for subdivision purposes; the second examines South African judicial decisions in the light of these principles. No attempt is made to discuss subdivision procedure in the four provinces of South Africa (1).

PART 1 - THE ECONOMIC PRINCIPLES (2)

The market value of a property will be dependent upon the income or occupational benefits that will accrue from its most profitable use. Where a property used or available at present for one purpose can be developed so that it will be more profitable if used for another, then the latter purpose will govern its market value. The best utilisation of the property, disregarding instances where social and private costs do not coincide, will be that which will be likely to yield the largest

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- (1) See Dönges and Van Winsen "Municipal Law", 2nd Edition, Chapter 21 for subdivision procedure in the Cape, and Estate Breet v. Peri-Urban Areas Health Board, 1955(3) SA.523 (A.D.) at 526, Estate Breet v. Peri-Urban Areas Health Board, 1955(3) S.A.534(T) at 537 to 539, and Florida Hills Township v. Roodepoort-Maraaisburg Town Council 1961(2) SA.386(T) at 388 for subdivision procedure in the Transvaal.
 - (2) The reader is referred to an article by R.L. Ward entitled "Taxation of Land Values in the Transvaal by Local Authorities", South African Journal of Economics, March 1942, in which there is an admirable discussion of township valuation at page 23 et seq. Together with other work of Ward this article has received less attention than it merited. See comment above, Chapter VI page 148. For an outline of the general principles of valuation see above Chapter II.

margin of profit (3). It is therefore necessary sometimes to consider whether the value of a property for subdivision purposes will exceed its value for sale to a purchaser for his own use.

The two basic approaches are the comparison or direct method and the detailed analysis or residual method. Although the writer considers it desirable to apply both methods where possible, there is usually little evidence on which the direct method can be based. This method proceeds upon a direct comparison of selling prices and is useful for the valuation of individual erven in a township, but there will normally be too many variables for townships as a whole to be directly compared (4).

In employing the detailed analysis method, account has to be taken of the steps required to convert land ripe for township development into subdivided sites. Firstly, it is necessary to predict the optimum future use having regard to the probable planning restrictions. An estimate has then to be made of the price at which it will be possible to sell the sites. By taking account of the time which will elapse before the plots can be sold and the various costs which will be incurred it is possible to derive a figure of value for the unsubdivided land from the prices which can be obtained for the plots.

Conditions prevailing in the neighbourhood and wider environment of the property must be considered in order to assess the optimum form of development. These will include the probable demand for plots, the existing supply of plots and probable future competitive subdivisions, availability of public services and the access to the property.

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(3) For a discussion of the social and private cost in land usage, see Chapter III pages 36-38.

(4) See references in Footnote (2) above.

In valuations of land for subdivision purposes it will usually be necessary for rough layouts to be prepared before approximate estimates of engineering costs can be obtained. Some discussion with local authorities will normally prove necessary. A major consideration in the valuation of land for township purposes is the delay before it will become possible to sell plots and the period over which the plots will be sold. Time is the all-important factor in the economics of subdivision. The developer should not budget for more than a reasonable share of future demand. In Robinson & Keeble's apt phrase, "the over-confident developer tends to bite off more than the public is prepared to chew" (5).

Apart from engineering costs, some allowance will usually have to be made for such items as professional services, legal charges, commission payment on sales, and advertising.

The net receipts from the sales of the plots must be discounted to give their present value (6). A township venture is speculative and a high rate of interest will have to be used. From the present value of the net receipts from the sales must be deducted the present value of engineering and professional costs and the present value of rates. One witness in the expropriation proceedings between City Deep Ltd. and the Johannesburg Municipality (7) submitted that the value of land for subdivision could be found by applying a percentage factor to the net receipts. This factor was not based upon compound interest calculations, but was a "rule of thumb" used to make allowance for all risk factors. Any procedure which confuses

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- (5) "Development of Building Estates", page 220.
- (6) This procedure is commonly known as the discounted cash flow or actuarial method. In South Africa because of its adoption in a case referred to below it is sometimes described as the Macfie Formula. See page 157 below.
- (7) August - September 1968. See Volume 32 of Evidence, and discussion below pages 175-177.

the element of time with other risk elements is likely to lead to inaccurate results. In so far as it is possible in investment analysis it is desirable to identify the risk elements and to provide for them specifically. As specific allowance can be made for the time element by the use of compound interest formulae these should invariably be employed.

The Municipal rates to be borne by the owner of the township (which will decrease as plots are sold) must be estimated and discounted to their present value. The effect of Municipal rates is usually somewhat problematic because the municipal valuation of the property may well be increased when it is declared a township and the assessment is difficult to predict (8).

Both Robinson & Keeble (9) and Lawrance, Rees & Britton (10) provide a lump sum for developer's profit as a form of cost. Robinson & Keeble specifically state that "the allowance is more properly dealt with as an addition to cost than as a deduction from receipts" (11). It is the writer's view that the expenses in each year should be deducted from sales in each year, that the net receipts should be discounted to their present value at a rate which allows for risk, and that the value of the undeveloped land be found by deducting initial expenses from the aggregate of the present value. It is preferable to regard the developer as an investor entitled to a high return on capital placed in a risk enterprise, rather than as an

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(8) See discussion below under heading "The South African Case Law".

(9) Op. cit. page 275.

(10) "Modern Methods of Valuation", 5th Edition, page 171 et seq.

(11) Loc. cit.

entrepreneur entitled to a profit (12), and it is customary to regard interest as the annual return on capital. This facilitates the comparison of alternative investments. Where a township development is spread over several years, an annual interest allowance can be made relatively easily; but in such circumstances it would be difficult to make a capital profit estimate because it is unlikely that there would be any evidence of similar allowances to serve as a basis of comparison (13).

Provision has to be made for the effect of income tax (14). The general rule is that the taxable income for each year will be con-

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- (12) Ward, writing in 1942 op. cit. page 24, states: "The rate of interest to be used, when capitalising the expected net income, varies in accordance with the risk involved. In practice, Municipal Valuers on the Witwatersrand seem to vary between 8 per cent and 14 per cent compound. Speculators, when buying a township, often use 'rule of thumb' methods, such as 'I must double my money in 5 years', which is equivalent to 15 per cent compound. In a town with a steady growth of population, 8 per cent would seem low, particularly when compared with the usual 6 per cent which is expected on first mortgage where not more than half the value of unimproved land is lent but the loan is secured against its full value. In a popular suburb of Johannesburg, 12 per cent would seem to be a fair rate at which to capitalise, but a higher figure should be used where the risk is greater."
- (13) With reference to the similar problem arising in building development schemes see above Chapter II pages 31-34. An alternative method might be not to load the discount rate but to treat risk separately, as a percentage (probability). For example, if the discounted sum at an interest rate regarded as "normal" is 100 and the chances of achieving it are 0.8 (80%), then $(0.8)(100) = 80$, which is the expected pay off. In terms of this approach in the formula
- $$\text{Value} = \frac{fp(1-t)}{1-ft}$$
- set out in Appendix A below, "t" would be a normal interest rate not reflecting risk and a probability factor would have to be applied to "p". To the writer's mind this method is more difficult to implement in practice than that set out in the text because risk allowance is inherent in any discount rate found in the market, and there is better evidence of variation in discount rates caused by differing risks than there is of probability allowances.
- (14) See Silke, "South African Income Tax", 5th Edition, page 781 et seq. See also Chapter II page 14 above.

stituted by the gross proceeds of the plots sold during the year less the sum of the original cost of the plots sold, development expenditure (e.g. roads) and current expenditure (e.g. rates). To find the original cost of each plot the total cost of the land must be allocated amongst the total number of plots which become available for sale. Instalment transactions are complicated by the rule that the whole of the sale price is deemed to have accrued to the seller on the day of entering into the agreement. The impact of this rule is, however, mitigated by the proviso that the Commissioner may make an allowance in respect of amounts which are deemed to have accrued but which are unpaid (15).

PART 2 - THE SOUTH AFRICAN CASE LAW

The decisions of South African courts in regard to land either subdivided into a township or having subdivision potential will be considered chronologically. The cases have arisen through disputes on valuation for either expropriation or rating purposes, principally the latter.

THE BRAAMFONTEIN CASE (16)

The first case in which the question of the value of township land arose appears to have been Braamfontein Co. Ltd. v. Johannesburg Municipality; it was certainly the first occasion on which the courts were required to consider the provisions of a rating ordinance in the Transvaal (17). From the official report of the judgment it appears that no judicial authority was cited to the court. The case is the foundation for subsequent decisions and remains even today the most important authority. It was a case stated under the Local

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(15) See Appendix A below for formulae to be employed in valuing land for subdivision.

(16) 1916 T.P.D. 745.

(17) See Florida Hills Township v. Roodepoort-Maraisburg T.C. 1961(2) SA.386 (T) at 392.

Authorities Rating Ordinance No. 6 of 1912 by Mr. T.C. Macfie, who was a Johannesburg magistrate. The judgment must be read together with that of Macfie to whom it was referred back and who was responsible for the actual assessment of value.

Macfie, fortified by the decision of the High Court, employed an ~~actuarial~~ (i.e. discounted cash flow (18)) calculation as one of the elements of his judgment, inter alia, as he says, "because both parties asked me to value on an actuarial basis", and "it was probably also the basis on which an intending purchaser would estimate what he would offer". The Macfie decision accords well with the economic principles set out in the earlier section of this chapter and represents to the writer's mind a sound approach to the problem. The actuarial approach to the valuation of township land has, however, not been accepted as a norm in any reported decision of the South African Supreme Court and it appears to remain open to the valuer to put forward any basis of assessment he may see fit. Indeed in *Florida Hills Township v. Roodepoort-Maraisburg T.C.* (19), Kuper J. referred to "a complicated calculation" which had been placed before the court and which dealt with the sale of the remainder; he stated that in his view "the court should not enter upon the method of calculation in regard to the remainder" and that "the valuer must be left as free as possible to exercise an unfettered judgment at the relevant time". To the writer this seems to be providing licence rather than discretion and it is a matter of regret that the courts have not entrenched the principles in the Macfie judgment by adopting an actuarial calculation as the normal basis of valuation of township land (20).

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(18) See page 153 above.

(19) 1961(2) SA.386 (T) at 398.

(20) In fairness to Kuper J., it should perhaps be noted that he was concerned with a case stated by a magistrate in terms of Section 15(1) of the Transvaal Local Authorities Rating Ordinance No. 20 of 1933 as amended, in terms of which appeals to the Supreme Court are limited to questions of law, and it may be that the judge's purpose in not considering the calculations submitted was merely to avoid the possibility of erecting any method of valuation into a principle of law.

The following passages from the judgment of Wessels J. in the Braamfontein case are set out and will be discussed below with reference to subsequent cases:

At page 747: "The valuer has to value the property in terms of section 7(1) of the amended Ordinance No. 1 of 1916 and he must value it according to the capital sum the property is expected to realise if offered at the time of valuation for sale on such reasonable terms and conditions as a bona fide seller would require. It is not the price which the seller puts upon the property that the valuer has to look to but the price it would fetch at a sale under such reasonable terms and conditions as any bona fide seller might require. It is the probable value of the property if put up for sale under reasonable conditions that concerns the valuer not the company's estimate of the value of the property."

And at page 748: "Suppose that the unsold stands in the township belonged to an estate and the executor or trustee had to wind up this estate what terms and conditions would he impose upon purchasers in selling the property - these would be more or less the terms and conditions that a bona fide seller would require in terms of the Act. That a bona fide seller would spread his selling over 20 years is unreasonable. This presupposes a capacity to hold up the bulk of the stands for an indefinite period. That is not the meaning of the reasonable terms and conditions under sec. 7(1) of the amending Ordinance."

And also at page 748: "The appellant's interest in the township should be treated as a unit in so far as the valuer has to ascertain the value of the interest as if all the stands are sold within a reasonable period as stands in a township and not as mere land of such and such dimensions. The stands are not to be valued on the basis of the price at which the appellants now offer a single stand or block of two or more stands for residential purposes. They are to be valued as if the company were a bona fide seller at the present time of all the unsold stands in its possession under such terms and

conditions as would be required where there was a bona fide intention to get rid of the interest."

THE GELDENHUYS (21) AND KLEINFONTEIN CASES (22)

The property in the Braamfontein case had already been subdivided; in the following year the question came before the court in the case of Geldenhuys v. Johannesburg Municipality of whether where land had a potential for subdivision it should be valued at a higher figure than its worth for farming purposes. The court held at page 244: "That an intending purchaser would be likely to take the factor of a possible subdivision into account cannot admit of any doubt. It is only natural that he would be prepared to give more for land which would lend itself to such subdivision than for land which would not. And it follows, therefore, that where this is possible the valuer is bound to take into consideration and give due weight to it" (23). This decision was followed in 1918 in the case of Kleinfontein Estate Township Company v. Benoni Municipality when the potentialities of a farm were taken into account for the purpose of assessing its value (24).

THE GLENCAIRN BUILDINGS CASE (25)

In 1926 the case of Glencairn Buildings Limited v. Johannesburg Municipality came before the courts. It was decided that in consequence of the terms of section 4 of Ordinance No. 1 of 1916, as

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- (21) 1917 T.P.D. 241.
 - (22) 1918 T.P.D. 193.
 - (23) It is to be noted that in all provinces of South Africa the principle of rebus sic stantibus (namely that for rating purposes property should be valued in its present usage) is not observed and rates are a tax on potential rather than actual use. See Chapter VI pages 136-137.
 - (24) For a discussion of the effect of the prospect of zoning change in the assessment of land value in expropriation law - see Chapter IV page 85.
 - (25) 1926 T.P.D. 68.

amended by section 5 of Ordinance 4 of 1917 (26), the four stands on which a building had been erected should be valued separately (27). The judgment at page 79 recognised that "an artificial position" was created by the Ordinance and stated that "the valuer is entitled to proceed just as if he had four stands in Johannesburg on which nothing had ever been erected, and is entitled to value them separately".

The decision of the court in the light of the unusual wording of the Ordinance and the particular facts of the case was probably inevitable, but it is regrettable that the judgment has subsequently been applied in other, and not analogous, circumstances. The essential words of the judgment were (28):

"And it seems to me that there is only one answer, namely, that if a person is a bona fide seller of 4 stands and he knows he will get a better price if they are sold separately rather than as a whole, then he will sell them separately and not as a whole. Therefore, we have to imagine a bona fide seller who is going to sell these 4 stands, and if it appears - as it does appear from the stated case - that the 4 stands sold separately would produce a higher price than if sold as a whole the valuer, in my opinion, is entitled to value them separately and to deal with them as though they were separate units."

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(26) The amended section reads: "Site value of land shall mean the capital sum which the land or interest in land might be expected to realise if offered for sale on such reasonable terms and conditions as a bona fide seller would require assuming that the improvements, if any, thereon or appertaining thereto, had not been made."

(27) It should be noted that the Ordinance does not enjoin the valuer to value separately every piece of land which is separately registered in a deeds registry. The effect of section 9(3), which refers to two or more contiguous pieces of agricultural land, in sum exceeding three morgen, is that any additional value arising from the fact that subdivision already exists may be ignored in the circumstances set out.

(28) Page 78.

It is submitted that this decision should be confined to its facts and that Ramsbottom J. in Randfontein Estates Gold Mining Co. (Witwatersrand) Ltd. v. Randfontein Municipality (29) interpreted the Glencairn Buildings case too broadly in stating:

"That case shows that an owner who owns several erven in a town is not entitled to claim that they should be treated collectively and valued as a unit." The test, in the writer's view, ought simply to be the market value of what is actually in the hands of the owner (30). In other words, what sales procedure will produce the best price and what will that price be? To repeat the words of the Glencairn Buildings judgment, if the "bona fide seller" of stands "knows he will get a better price if they are sold separately rather than as a whole, then he will sell them separately and not as a whole". Conversely, if the bona fide seller knows that he will get a better price if the stands are sold as a whole rather than separately, then he will sell them as a whole and not separately - and they ought to be valued as a whole. If the realities are that he is holding "township land" (31) for sale then this should be recognised as his stock-in-trade and valued on this basis - no matter whether or not he is the original township owner, or whether he has acquired the township owner's interests as such (32), or whether he has merely acquired a group of erven with a view to resale. The test is thus not whether stands are registered separately or under one title in a Deeds Registry, but

(29) 1939, T.P.D. 406 at 410.

(30) See extract below, page 162 from Braamfontein Case at 747.

(31) See use of this term in Randfontein Estates Gold Mining Co. (Witwatersrand) Limited v. Randfontein Municipality 1939 T.P.D. 406 at 418. Normally in the case of "township land" the best price would be achieved by the sale of the erven as a unit to a person who intended to hold the erven for sale over a period, and not by selling the erven on one day in competition with each other to different purchasers.

(32) For a discussion of the meaning of the term "township owner's interest" see Rynfield Township Ltd. v. Benoni Town Council and another, 1950(4) SA.717 (T) at 722 and Estate Breet v. Peri-Urban Areas Health Board 1955(3) SA.534(T).

what is the real value and nature of the interest in the hands of its present owner. If the test were not the realities of the value of the owner's asset, but the manner of registration of the title (i.e. whether separate or collective) manifestly absurd results could follow. Assume that a township is subdivided into 1,000 stands, that the stands are selling for a price of R1,000 each, and that a valuation of the township on an actuarial basis shows it to be worth R300,000. Should the test of registration be applied without regard to the true nature of the owner's asset, he would pay rates on R1,000,000 or on R300,000 depending merely upon whether the stands were registered under one title or separately. It is admitted that under the test of economic reality marginal cases would arise, but the test is factual and presents no particular difficulties to the valuer. The matter was put with clarity by Wessels J. in the Braamfontein case at pages 747-748:

"Mr. Lucas (for the Johannesburg Municipality) would take a particular stand and value it on the basis that all other stands are firmly held by the company; in other words as if the only competition at the sale of a particular stand were the stands already sold and available for purchasers and such of the other stands as would be likely to find purchasers at the time when the stand to be valued is dealt with. This set of circumstances he would assume at the sale of every stand. The value of each stand would therefore not be determined by the present value of all the stands in the hands of the company but by the fact that the company is keeping up the price of the stand by fixing on each of the other stands a price higher than its normal value. This would not be fair to the company nor would it be a valuation based upon the valuer's judgment as to what the interest of the company in the township could be expected to realise if offered for sale at the time of the valuation. It would be a value of one stand on the basis that the others are withheld from the market for a considerable time. The valuer must put a value on the interest of the company in all unsold stands on the assumption that all the stands are to be sold on such reasonable terms and conditions as they would be sold under if the Braamfontein Company resolves to sell its interest in the township."

It is to be noted that the judgment made no reference to the manner of registration in a Deeds Registry and was concerned with the economic realities of the "interest of the company". Wessels J. clearly understood that value was the equilibrium point between supply and demand (33) and that the valuer had to consider what the available supply of erven would be at the time of his valuation. Depending on the assumptions adopted by the valuer in respect of supply different conclusions as to the value would be reached. The judge rejected the proposal of Mr Lucas and held that the valuer must assume that the company would adopt a rational policy in the disposal of its interest (34).

THE CORONATION CASE (35)

The next case of importance is the unreported decision of Coronation Freehold Estates, Towns and Mines Limited v. Balfour Village Council. In this case a township was proclaimed and a number of erven were reserved to one McHattie (36). He then transferred some of these erven to a company which in turn transferred some of the erven it received to the appellant which subsequently sold some of the erven it had bought. The stands had been valued separately and the appellant contended that its unsold stands should be valued as a unit - a contention which was rejected by the court. The decision might have presented less difficulty if it had proceeded on the basis that the appellant was not the township owner and that therefore the erven

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- (33) See Chapter II at page 6.
- (34) See discussion of the concept of "floating" value propounded by the Uthwatt Committee in Chapter V page 105 above.
- (35) T.P.D. September 29, 1937.
- (36) See Randfontein Estates Gold Mining Company (Witwatersrand) Limited v. Randfontein Municipality, 1939 T.P.D. 406 at 416.

should have been valued separately (37), although this would have led to an equally infelicitous result. In fact the argument seems to have been on the basis that the appellant was the township owner, as in the Braamfontein case, and the Braamfontein case was interpreted as requiring the valuer to value separately the unsold stands in a township while held by the township owner under township title. That the decision was confused appears from the admission of Barry J., one of the judges in the Coronation case, in his subsequent judgment in the Randfontein Estates case at page 421. It is submitted that the observation of Ramsbottom J. in the Randfontein Estates case at page 416 is correct when he says "that the views expressed in the Coronation case may have to be reconsidered".

THE CAPE AND TRANSVAAL CASE (38)

Unfortunately, in the year before the Randfontein case the Coronation case had been followed in the Cape and Transvaal Land and Finance Company Ltd. v. Director of Valuations. Centlivres J. at page 448 states that he agrees with the decision arrived at in the Coronation case and that "in effect the Court held that the case of Braamfontein Co. Ltd. v. Johannesburg Municipality is not an authority for saying that where land is held by a company which sells the land in plots and where that land has been subdivided into plots that it should be valued as a unit". The interpretation placed by the court on the judgment in the Braamfontein case is not easily understood. Centlivres J. appears to be of the opinion that the Municipality's contention in the Braamfontein case was rejected because, to quote his words, "it appeared from the facts in that case that the company

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(37) A procedure which was subsequently regarded by Ramsbottom J. in the Randfontein Estates case at page 416, erroneously it is submitted, as having been the ratio in the Glencairn Buildings case. Kuper J. also places this interpretation on the Glencairn Buildings case in the Florida Hills case at page 394.

(38) 1938 C.P.D. 441.

fixed what I may describe as an artificial price in selling its lots" (39). He states: "That is, the company kept up the price of the stands by fixing on each of the other stands a price higher than their normal value" (40). Now, with respect, that is not the point of the Braamfontein case at all and the judge's interpretation of the case is attributable to an erroneous apprehension of the operation of the land market. It is submitted that the difficulties that arose in the Coronation case and in the Cape and Transvaal Land case stem from failure to confine the decision in the Glencairn Buildings case to its own facts.

Kuper J. in the Florida Hills case at page 394 quotes the Coronation case as stating: "It is quite clear that the effect of that decision (i.e. the Braamfontein case) is not that the unsold stands are to be treated as a unit and valued in a lump sum, but that each stand is to be valued as if the company were a bona fide seller at the time of valuation". He observes, correctly in the writer's opinion, that this was not an accurate statement, for the court in the Braamfontein case had dealt with the valuation on the basis of all the stands being sold over a reasonable period of time and not on the basis of each stand being dealt with separately. He goes on to say that in the Cape and Transvaal case no distinction was drawn between the principle laid down in the Braamfontein case on the one hand and the Glencairn and Coronation cases on the other, making the point that the Coronation case should have been based upon the Glencairn because the appellant in the Coronation case was not the township owner - a contention with which the writer does not agree as has been indicated above. It would seem from page 395 of Kuper J.'s judgment that he is of the opinion that in order for the owner of the stands to escape having them rated separately he must not only be a township owner but must be the 'original township owner'. This view led Kuper J. at page 399 to conclude that some thirteen erven could not be valued

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(39) At page 447.

(40) Ibid.

with the remainder but had to be valued separately, a point to which we shall return below when considering the Florida Hills case in more detail.

THE RANDFONTEIN CASE (41)

The judgment in Randfontein Estates Gold Mining Company (Witwatersrand) Limited v. Randfontein Municipality, which was given in the year after the Cape and Transvaal case and two years after the Coronation case, did something to rectify the confusion which had been created. The headnote in the Randfontein case reads:

"A valuer, acting under the provisions of section 9(1) of Ordinance 20 of 1933, must place upon the valuation roll and value as a unit the whole of any piece of land which is registered in the Deeds Register as one property. In making such valuation he can take into consideration the fact that the property is likely to fetch an enhanced price through being easily capable of subdivision, or, alternatively, he may take a notional subdivision and assess on the basis of what the whole would be expected to fetch if offered for sale in separate portions at one and the same time, namely the time of valuation; he is not entitled to divide up and enter such property upon the roll as separate areas each being valued according to the use at (sic) which it could be put at a price which it would be expected to fetch if sold separately in point of time from the remainder."

Referring to the Braamfontein case, Ramsbottom J. at page 418 says that the valuer is not to value land as "mere land of such and such dimensions" but as "township land" which has been laid out into stands which can be sold separately. He states: "This means, I think, that the land had valuable potentialities; the owner had received the statutory privilege of cutting up the land into plots which were available for sale and transfer to purchasers, and the purchaser

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(41) 1939 T.P.D. 406.

of the interest would have the same right". In making his calculation the valuer has to value the stands as if the company were the bona fide seller at the present time of all the stands "under such terms and conditions as would be required where there was a bona fide intention to get rid of the interest". This, in Ramsbottom J.'s view, was the sense in which the judgment was understood at the time by Macfie and the sense in which it had been acted upon ever since. He concluded that the Braamfontein case is therefore not in any way an authority opposed to the contention that the property must be valued as a whole (42). At pages 418-419 Ramsbottom J. states, without expressing a decisive opinion, that there may be "an important difference between land which has been laid out as a township and cut up for sale in lots, and land which has not been so laid out". Looking to the economic principles set out in the first part of this chapter, it can be seen that there is, however, no essential distinction and that the same valuation procedure is applicable whether land has been subdivided or whether it merely has a potential for subdivision - although clearly in the latter case the risk element is greater and the value will be less (43).

At page 420 Ramsbottom J. states that there are two possible approaches to valuation: "What must be determined is the sum which the whole might be expected to realise if offered for sale in portions at the time of the valuation. Or the valuer may adopt an alternative method. He is entitled to say that a reasonable seller would offer the whole farm for sale as a unit, and that if so offered the price which it would fetch would be enhanced by reason of the fact that it could easily be subdivided".

Again looking to the economic principles set out in the earlier part of this chapter, it is apparent that the same calculation would be

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 (42) c.f. the view of Centlivres J. quoted at page 164 above.

(43) See comment by Ward, op. cit. at page 26.

employed whichever "method" were adopted, and that there is in reality only one approach to the problem. Regrettably some importance seems to have been attached to this supposed distinction in methods of valuation. In the Florida Hills case at pages 395-399 Kuper J. was at some pains to decide which method was applicable "in the special circumstances" (44) of that case.

S.A. RAILWAYS v. NEW SILVERTON (45)

The case of S.A. Railways v. New Silverton Estate Ltd., appears to be the first recorded case in South Africa in which the problem of township potential had to be considered where the dispute arose out of an expropriation rather than a rating assessment (46). It also seems to have been the first case in which the Appellate Division was required to consider the problems of the value of land for subdivision. The court held (47):

"The issue in the present case is not the value of the land as agricultural land but 'an increase accruing to the value of the land by reason of its potentialities or possibilities', to use a phrase in the judgment in Sri Raja v. Revenue Officer (1939, 2 A.E.R. 317 page 320). The potentiality of any added advantage due to existing possibilities of development is a proper subject for consideration. The company's case is based on the potentiality of the land as a township. But obviously there is much uncertainty in the factors bearing on such potentiality, and the learned Judge had to make an estimate of such factors in the light of the evidence."

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(44) See page 397.

(45) 1946 A.D. 830.

(46) See generally Chapter IV and in particular, the discussion of admissibility of evidence of potential change in zoning at page 85.

(47) At page 838.

The judgment of the lower court, in so far as it turned upon taking account of the potential of the land for subdivision, was confirmed.

KRAUSE v. S.A.R. & H. (48)

The case of Krause v. S.A.R. & H. is also an expropriation case and provides a precedent for arriving at the value of undeveloped land by considering its potential value if subdivided for industrial use. At page 560 De Beer A.J.P. sums up the principle in the Sri Raja case as follows: "Die potensialiteit moet vasgestel word op die beskikbare gegewens 'without indulging in feats of imagination': die oorwegings sluit in tot seker mate die moontlikheid dat die potensialiteite miskien eers na jare, miskien nooit ten volle, verwesenlik sal word nie". The court concluded that the land had a potential for both residential and industrial subdivision, and that the owner was entitled to the higher value which, in the circumstances, was that based on industrial usage (49).

THE FLORIDA HILLS CASE (50)

We come now to the judgment in the Florida Hills case, to which reference has already been made and which has added no little to the confusion of the principles upon which land either subdivided or with subdivision potential should be valued. Unfortunately the words already quoted above (51) from the Braamfontein case at page 748 to the effect that it should be assumed that the unsold stands in a

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(48) 1948(4) SA.554 (0).

(49) See page 570.

(50) 1961 (2) SA.386 (T). This case was preceded by the arbitration proceedings between Lenz Township Company (Pty) Ltd. and Group Areas Development Board in which the problem of township valuation was involved. The report of the arbitrators dated 23rd February, 1960, contains some unusual valuation calculations for which the writer knows of no precedent and which do not seem to require discussion.

(51) See page 158 above.

township belong to an estate and the executor has to wind up this estate were open to misleading interpretation and led Kuper J. at page 397 to conclude that "the valuer should fix the reasonable period of time within which the erven would be sold - not to the best advantage for that might take a considerable time but within the period envisaged in the Braamfontein case, namely that taken by an executor or trustee to liquidate the assets of an estate". The further observation of the judge at page 397 to the effect that it was not clear to him "why any period of time should be allowed, and why the valuer should not be confined to a valuation on the basis of a sale of all the erven in competition with each other on the 30th June, 1959" seems indicative that the essential principles of valuation were not drawn to his attention. The procedure which he contemplates would lead in all probability to a material part of the value of the asset being thrown away.

In the Randfontein case it had been held that "the valuer is entitled to consider what the best way of disposing of the whole would be if it were offered for sale at the time of valuation" (52). That Kuper J.'s above dicta on the period of selling in the Florida Hills case were irreconcilable with this statement in the Randfontein case, does not seem to have been apparent to the court in the subsequent case of Steelpark Estate Company Ltd. v. Vereeniging Town Council (53), because after some discussion of the Florida Hills case Jansen J. quotes this passage from the Randfontein case with apparent approval. However, in the subsequent case of Risi Investments (Pty) Ltd. v. Vereeniging Town Council (54), which has served to bring back some clarity to the law, Clayden J. observes at page 313: "The reference by Wessels J. (in the Braamfontein case) to the conditions which, say, a trustee in an estate might impose on purchasers, is not in my view

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(52) Page 420.

(53) 1963(2) SA.367 (T) at 376.

(54) 1965(3) SA.307.

to be read, as is argued, as meaning that the seller would insist that the purchasers sell fairly quickly, or indeed in any particular manner. The judgment of Wessels J. was explained by Ramsbottom J. in the Randfontein Estates case I do not propose to repeat that explanation". Similarly, Galgut J. in the Risi case at page 311 states that: "This argument overlooks the fact that Wessels J. in the Braamfontein case was dealing with a case where the township owner was deliberately spreading the sales over twenty years. The learned Judge pointed out that a reasonable time for a disposal of the stands should be allowed. What is reasonable will depend upon the evidence".

From the following statement by Kuper J. in the Florida Hills case at page 393, it would seem that he is of the opinion that Macfie did not act in accordance with the Braamfontein decision:

"Although it is clear from the judgment that the Court dealt with the valuation on the basis that all the stands would be sold to many purchasers over a reasonable period of time, the magistrate to whom the detailed valuation was referred dealt with it on the basis of ascertaining what sum one purchaser would be fairly expected to give for the whole of the unsold stands if offered for sale at the time of valuation on the terms and conditions and with due regard to the considerations mentioned in the Ordinance". In the writer's opinion this does less than justice to Macfie whom it is submitted had a fair assessment of the valuation principles involved and avoided the pitfall into which the courts have subsequently fallen of thinking that there were two methods of valuation which would produce different results.

Kuper J.'s failure to appreciate that the two "methods" of valuation embrace the same calculations and reach the same conclusion is most clearly evidenced by the following passage at page 396 of his judgment: "In the case, therefore, of an established township the valuer is entitled to adopt either method in order to arrive at a proper valuation and in suitable cases he will no doubt apply both methods, the result in each case acting as a check on the other. In some cases it may prove extremely difficult to apply one or other of the methods and in

such cases the necessities will compel the adoption of the only practical one."

That he also fails to understand that all the valuer can do is to process the available evidence and that the accuracy of any valuation will be dependent on the comparability of the data available is clear from his statement at page 397 that: "The valuer would experience no notional difficulty in appraising the value of the remainder. It is true that he might not be able to assess the value on the basis of comparative sales or on the basis of obtaining the evidence of what a willing buyer would pay for the property but on the basis of the evidence of experts it should be possible to ascertain the value of the property". The writer, at least, would find himself unable to be of help to a court where there was no data upon which he could base his testimony. Valuation is founded upon economic analysis which can be presented in written and logical form to a court and is not an esoteric art. The judge's conclusion at page 398 that "the only practical method of valuing this township in its state of development on the relevant date is by ascertaining the capital sum which the remainder would be expected to realise if offered for sale" takes the matter no further and does not in reality supply any answer at all, the "capital sum" being dependent upon the "complicated" calculation which the judge felt the "court should not enter upon" (55).

At page 399 in regard to 13 erven held under separate title (56) the judge stated that the valuer should make a separate valuation in regard to each erf. This is presumably on the basis of his interpretation (57) of the Glencairn Buildings case although it is not stated so to be. The judgment goes on to say that no allowance need be made for any

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(55) See comments above at page 157.

(56) For the reason that the Rand Townships Registrar required such certificates to be taken out before he would register certain servitudes required for sewerage purposes. See 390.

(57) At 394.

commission paid to agents or to any selling expenses or to advertising. This seems manifestly incorrect but according to the judge the valuer should apply the test stated in the Braamfontein case, although what he understands to be this test is not clear from the text. Kuper J. says that it would be wrong for these 13 erven to be included with the remainder as the "factual position is different and it is the factual position which must be dealt with by the valuer." In the writer's submission factually the 13 plots were no different from the remainder as the purchaser would be buying them with the remainder as part of a township.

With regard to the conclusions in the judgment at page 400, it may be understandable that erven which have been sold but have not yet been transferred should be separately treated, but it is not clear why this should apply to erven so sold but of which the deeds of sale have been cancelled. Nor is it understandable why "no allowance should be made in respect of the expenses actually incurred by the township owner in respect of such sold erven either in carrying out the obligations imposed upon it by the conditions of establishment of the township or in maintaining, developing and selling the same".

THE STEELPARK CASE (58)

The judgment in the case of Steelpark Estate Company v. Vereeniging Town Council also has unsatisfactory features. The valuation of a Mr Kruger is cited with apparent approval at pages 374 and 375. Mr Kruger based his "gross valuation" on the owner's price list (59). From this figure Mr Kruger deducted a sum although no actuarial

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(58) 1963 (2) S.A. 367 (T).

(59) It may be observed that it is unusual in real estate transactions to get the full price for which one asks and it is therefore somewhat optimistic to assume that the prices asked would have been achieved in every case.

calculation was set out to explain the bases for this deduction. He then proceeded to draw an analogy between the erven in a township and the township on the one hand and the cattle in a herd and the herd on the other, apparently not recognising the mobility of cattle, either dead or alive, and the fixity of land, or the totally different marketing problems attaching to an erf which is always in some respects unique and meat which is typically a fungible.

The basis upon which Mr Kruger reduces his "gross valuation" to his final figure is not clear. The judgment at page 375 states that:

"In arriving at the net values of the erven he valued them all on the basis of them (sic) being offered for sale at the same time."

However the judge goes on at page 376 to say:

"It would seem that in substance Mr Kruger did value all the land as one unit: the total of his values allocated to individual erven is not the total value of the erven valued as separate units, but the total value of all the erven valued as one unit."

It has been observed above: "In real estate valuation, the 'thing' to be valued is the group of rights attaching to a property (60).

The observation of Jansen J. at pages 376 and 377 to the effect that the unit being valued is essentially corporeal land and not an incorporeal, consisting of rights and obligations, denies the economic realities. The writer finds no substance in the statement of the judge that: "The recognition of the method of notional sub-division in respect of the property of a township owner is indicative of the fact that the unit to be valued is land (in italics), and not an abstract concept of 'township owner interest' - were it the latter, the only appropriate method of valuation in all cases would have been the other." The term 'other' has reference to the alternative 'method' of valuation which was supposedly employed in the Florida Hills case.

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(60) See Chapter II page 6.

THE RISI INVESTMENTS CASE (61)

The final case is that of Risi Investments Ltd. v. Vereeniging Town Council which, as has been stated, resolved some of the confusion in this branch of our law. It was decided that, in terms of the Local Authorities Rating Ordinance 20 of 1933, it was permissible in calculating the value of the township owner's interest in respect of the unsold stands in the township to have regard to the estimated assessment of rates payable in respect thereof. The court rejected the argument that section 9(1) differed from other statutes in that it referred to the "bona fide seller" and did not refer to the purchaser. At page 311 Galgut J. stated that: "This argument loses sight of the fact that the section requires the fixing of a capital sum to be expected at the notional sale. It is only the reasonable terms and conditions which a bona fide seller would require which are referred to in this section. The section makes no mention of the price the seller demands or requires". The judge refers in this regard to the passage from the Braamfontein case at page 747 quoted above (62).

THE ARBITRATION PROCEEDINGS BETWEEN
CITY DEEP LIMITED AND JOHANNESBURG
CITY COUNCIL (63)

These proceedings concerned the expropriation of part of the site of City Deep Limited for a market by the Johannesburg Municipality. Although the optimum use of the land in economic terms was for subdivision into industrial sites, government policy, and in particular the Physical Planning and Utilisation of Resources Act No. 88 of 1967 (64), made it uncertain as to whether permission for industrial use could be obtained. The evidence of witnesses as to the effect

.....
(61) 1965(3) S.A. 307(T).

(62) See page 158 above.

(63) Arbitration award 31.12.68.

(64) See Chapter III page 50.

of the passing of the Act on the prospect of obtaining industrial rights was very divergent. The arbitrator came to the conclusion that whilst the weight of evidence showed that a prospective seller and purchaser would not have negotiated on the basis of a probable industrial potential he was justified in allowing a comparatively minimal amount for the prospect of obtaining industrial rights (65). The figure arrived at by the arbitrator fell between the offer of the Municipality and the claim of the owner, but the method of calculation employed is not clear (66).

A further difficulty which faced the arbitrator is that in all probability no unconditional transaction would have been concluded by the seller and the purchaser because neither would have wished to have final commitment until the question of industrial rights had been settled (except on a basis which would have been so unfavourable to the other party as to be unacceptable).

Turvey's analysis of ceiling and floor price is instructive although it provides no solution to the question confronting the arbitrator: "Let a person's (or a firm's) Ceiling price for a particular interest be defined as the maximum he would be prepared to pay for that interest; it will be different for different persons. Let the owner's Floor price for a particular interest be defined as the minimum sum

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- (65) See pages 51 and 52 of the Award. This was a somewhat more pessimistic view than that taken in the earlier arbitration of M.G. Karam (Pty) Ltd. v. Johannesburg City Council which concerned land adjoining the City Deep property. The closing arguments in the Karam Arbitration were presented on 18th April, 1968; the City Deep hearing commenced on 24th June, 1968.
- (66) The arbitrator misunderstood the evidence of the writer in that it appeared to him that the method employed (which is that set out in Appendix A below) did not recognise that the investment would be not only the purchase price of the land but the development costs. The arbitrator also seems to have thought that the 12% before tax discount factor employed at one stage of the calculation allowed only for a lump sum profit of 12% and not for 12% compound per annum on the outstanding balance of the investment. See page 85 of the Award.

for which he would be prepared to sell that interest. Then it follows . . . that a particular interest would be sold if one or more persons have a Ceiling price greater than the Floor price. If only one person has a Ceiling price in excess of the owner's Floor price, the price realised will be somewhere in between. If there are more than two persons prepared to offer a sum acceptable to the owner, the price must lie between the two highest Ceiling prices, since the purchaser will have to outbid his rivals" (67).

It can be seen that a transaction in the market takes place when the Ceiling price of the purchaser is above the Floor price of the seller, and that when the seller's Floor price is above the buyer's Ceiling price (as would in all probability have been the circumstances if there had been negotiations for the City Deep property before the feasibility of industrial rights was established) no transaction takes place. Under these conditions the valuer can be of little assistance to a court and there is no escape from an arbitrary decision based upon the court's speculation about the prospect of rezoning.

CONCLUSION

The difficulties facing the courts have arisen because, despite the salutary example of the Braamfontein judgment, basic valuation principles have not been grasped. It requires to be understood that (in the absence of evidence upon which to base the method of direct comparison) there is in reality only one method of valuing township land or land with township potential and not two as was thought in the Florida Hills case. Moreover, the discounted cash flow method, the so called Macfie formula, should be upheld as the correct approach to valuation. In all cases what should be valued is the effective economic interest in the hands of the owner, and the method of registration in a deeds registry should be disregarded as being irrelevant.

.....
(67) "The Economics of Real Property", page 8.

The need for a specialist division of the Supreme Court to adjudicate real estate valuation cases is demonstrated by the present inability of judges and arbitrators to understand the application of economic principles in which they have typically had neither experience nor training (68).

APPENDIX A : FORMULAE FOR VALUING
LAND WITH TOWNSHIP POTENTIAL

It is evident that the value of a site for subdivision is the present value of the proceeds from plot sales after deduction of the present value of all expenses (not including original cost of land) and taxation. The value of the unsubdivided land can be found by the following formula (assuming no instalment sales):

Let x = Value including price and transfer costs (if any) (69).

f = Factor for Present Value of R1 (allowing for effect of tax on compound interest accumulation) receivable at the end of period, this period being from date of purchase of unsubdivided plots to midpoint of plot sales.

p = Total proceeds of plots less expenses incurred coincidentally with sales.

t = Amount of income tax per rand expressed as a decimal function.

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(68) See comment above Chapter VI page 147.

(69) It should be noted that market value is the sum of the predicted purchase price and any transfer costs which may be incurred. To the extent that transfer costs are incurred the purchase price will be less than market value. Transfer costs are part of an owner's investment and if his property is expropriated he should be compensated at market value and not predicted selling price; similarly he has no grounds for complaint if his rates assessment is based on value, including transfer costs.

R = Present value of rates (70).

e = Expenses other than x and those allowed for in p and R (e.g. road development costs which must be incurred before sale of plots can commence).

F = Factor for Present Value of R1 (allowing for effect of tax on compound interest accumulation) receivable at end of period, this period being from date of original cost to mid-point of incidence of costs allowed for in "e".

$$\begin{aligned}\text{Then } x &= fp - ft(p - x) - Fe(1 - t) - R(1 - t) \\ &= \frac{(1 - t)(fp - Fe - R)}{1 - ft}\end{aligned}$$

It should be noted that R is the sum of the Present Values of the rates paid in successive years during the period in which plots are being sold. In order to find R,

Let A = Factor for present value of R1 receivable at end of first year.

B, C, etc = Same for succeeding years.

a = Rates payable in first year.

d = Decrease (assumed to be constant) in rates in each successive year.

$$\text{Then } R = Aa + B(a - d) + C(a - 2d) \text{ etc.}$$

.....

(70) The figure "R" is a rough estimate. It would be possible to construct a formula which would make rates a percentage of "x", but in the light of the relatively negligible consequence of inaccuracy in the figure for rates the additional complexity in the calculation occasioned by this refinement would not be justified.

For most practical purposes the simpler formula set out below will be adequate:

$$x = \frac{fp(1-t)}{1-ft}$$

Where x = as above
 f = as above
 t = as above
 p = total proceeds of sales less expenses incurred coincidentally with sales and expenses incurred before sales (allowing for interest accumulation from date expenses incurred until midpoint of plot sales).

NOTE

The formulae are based on the assumptions:

- (a) that the interest income arising from an investment of the sum x would be taxable over the period and accordingly a rate of interest net of taxation should be used, i.e. if V were the value of R1 at a gross rate of interest of I, then f is the value for the same period of R1 at a net rate of interest of $I(1-t)$.
- (b) that tax would have been paid on the excess of the net proceeds (net of expenses) over the "purchase price" and that the present value of an amount supplied to provide such tax would have been taxable as to the interest earned thereon. The present value of such taxation represents a deduction from the value of the land.

Provided the period under consideration is relatively short (say, not more than ten years) and that plot sales are effected at a reasonably uniform rate, it is a fair approximation to apply discount factors on the assumption that all transactions take place at the midpoint of the selling period.

CHAPTER VIII

RENT CONTROL

INTRODUCTION

In several countries, including Britain, France, the United States and South Africa, the first general application of rent control occurred either during the First World War or in the housing shortage following immediately thereafter. The first South African legislation was the Tenants' Protection (Temporary) Act, 1920 (1), which was followed in the same year by the Rents Act (2). In the United States rent control has been recognized by the courts as a legitimate exercise of the police power (3) and has generally been thought to be an emergency measure to deal with a temporary situation. Rent controls were in fact abolished in the United States in the 1920s, and were not reimposed until the Second World War. As a national measure the regulations were subsequently repealed, but in one State, that of New York, they still remain in respect of residential property by virtue of State legislation. In Britain the legislation was originally commonly regarded as an emergency device to remove hardship and forestall inflationary wage claims (4), but in that country, as in France and South Africa, some form of rent control legislation has remained in force.

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(1) Act No. 7 of 1920.

(2) Act No. 13 of 1920.

(3) For a discussion of the concept of "police power" see above, Chapter V pages 109-110 and 114.

(4) See Macrae, "To Let" page 3 and Needleman, "The Economics of Housing", page 162.

THE CASE FOR RENT CONTROL

The price of any commodity in a private enterprise economy is a function of the interaction of the forces of supply and demand. Rent is the annual price paid for space; the capital value of space is dependent upon the level of its rent and upon its quality as an investment in respect of risk, liquidity and ease of administration. It is apparent that where the controlled rent of a property is less than the price that the landlord could have obtained for the space in the absence of control, the value of the property will also be less. In the United States as the courts have accepted rent control as an exercise of the police power of the State the question of compensation for that part of the value of the property which is in effect expropriated has been avoided; nor to the writer's knowledge has compensation ever been paid elsewhere. Rent control is thus tantamount to taking property without compensation (5). The justification for so doing can only be based on the premise that such part of the rent as is in excess of the amount established by control would, in the absence of control, have transgressed the prevailing moral code of the particular society.

It is a principle of a free economy that excess demand for any commodity will lead to an increase in supply and the resulting competition will eliminate excessive reward to the owner of that commodity. Similarly, inadequate reward will be rectified by a contraction in supply and a consequent decline in competition. However, the supply of accommodation is relatively slow to respond to an increase in demand and requires a longer period of time than almost any other commodity to adjust to a fall in demand. It is therefore to be expected that at times landlords will be in an advantageous

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(5) Alternatively, Rent Control might be regarded as a tax imposed upon the owner of controlled property by the state and distributed to the tenants of such property.

bargaining position vis-à-vis tenants and that at other times tenants will have the upper hand. Rent control may be justified when the position of the landlord has the characteristics of quasi-monopoly; similarly, in a reverse circumstance a case could perhaps be put forward for subsidizing landlords, but to the writer's knowledge this has never eventuated. Justification for rent control might exist where alternative accommodation was not available to the tenant, and subsidies to landlords might be justified where a down-turn in the economy resulted in the supply of accommodation exceeding that which could be let at rents giving a fair return on cost. The inability of the poorer members of a community to pay an economic rent for housing may provide good grounds for State subsidy but is no reason for rent control (6).

Rent control will have its strongest foundation where war or other emergency conditions suspend the normal operation of market forces. Where, for example, building control in time of war creates an artificial restriction in the supply of housing, landlords will be able to obtain rents above those which would prevail if the supply of

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- (6) A scheme for State subsidy based on an annual means test is put forward by Jane Jacobs, "The Death and Life of Great American Cities"; see Chapter 17. See also Needleman op. cit. page 167 et seq. Subsidising the cost of housing through loans at rates of interest below those at which the government itself borrows is standard practice in the U.S.A. and Western Europe as in South Africa, but not in Britain. It is of interest that despite 50 years of rent control in Britain in a survey conducted in 1967 64% of the persons interviewed considered that rents should be freed and the poor helped. In the opinion of 76% of the persons interviewed aid to the needy should be based upon a means test. See Pennance and Gray "Choice in Housing" pages 18 and 20. Western Germany has developed, alongside progressive decontrol of rents, one of the most sophisticated systems of selected housing aid in which cash payments are made to individual households thus enabling them to choose for themselves the quality and location of dwelling best suited to their needs. See Pennance and Gray op. cit. page 68. A recent research study in Britain by Gray, "The Cost of Council Housing", reaches the conclusion that no future public house-building should be subsidised.

building were permitted to respond to the demand for accommodation (7). When the control suspending the erection of new housing is removed (and when, if they had been imposed, wage increase restrictions and control of the prices of commodities other than space are removed) the justification for rent control will disappear. It is precisely because rent control has been retained when other controls have been removed that it has so often been attacked as an unjust imposition upon the owners of property. To the writer's mind the only circumstance where rent control can be justified is where abnormal economic conditions prevent the normal response of the supply of space to the demand for space. Cyclical fluctuations in the economy which are not of abnormal proportions may enable landlords to charge higher rents at certain periods than at others, but they do not form ground for rent restriction any more than they do for subsidy to landlords. It is to be admitted that to a limited extent and for a limited period a landlord could exact from a sitting tenant a higher rent than he could obtain from a new tenant (because the former would wish to avoid such inconvenience and costs consequent upon the termination of his lease as would flow from a search for new accommodation, moving, a change of telephone number, loss on carpeting and the like), but it would be a foolish landlord who seized upon such a short-term advantage over a tenant, for such practice would hardly be conducive to maximizing the income from the property over a period.

THE CRITICISMS OF RENT CONTROL

There are several grounds upon which rent control is to be criticized (8).

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(7) Whilst rent control in such conditions of housing shortage will prevent the exploitation of tenants by landlords, it tends to exacerbate the shortage of accommodation because if landlords had been permitted to raise rents individual tenants would have taken less space and others would have been allowed to share the available accommodation.

(8) See generally Turvey, "The Economics of Real Property", pages 43 ff.

One of the main advantages of property as an investment medium is that its nominal income adjusts to changes in the purchasing power of money in the absence of interference with the price mechanism. The usual effect of rent control is to remove almost entirely this attraction from property. Rents are fixed and real income (i.e. the purchasing power of the rent received) falls as inflation takes place. The objections against rent control are that it causes an arbitrary redistribution of real income in favour of tenants of rent-controlled accommodation and against their landlords; it decreases the ability of landlords to maintain their properties in good condition, thus reducing the useful life of buildings and creating slums; it discourages the owners of existing properties from letting as opposed to selling; it deters the development of new buildings; it arbitrarily diverts expenditure from property maintenance and development to other sectors of the economy; it disrupts the allocation of accommodation by the price mechanism and leads to simultaneous overcrowding and under-occupation; consequent upon the underconsumption of controlled accommodation, it leads to increases in the demand for and costs of non-controlled space; and it impedes the geographic mobility of labour because people are reluctant to leave accommodation which they occupy at less than market rentals. Some of the above criticisms of rent control will be discussed in further detail below.

INJUSTICE TO OWNERS OF CONTROLLED PROPERTY

The subsidies received in effect by the occupants of rent-controlled accommodation come not from the body of taxpayers as a whole but from those investors who happen to have been sufficiently unfortunate to place their funds in property rather than in some other investment medium. This redistribution of income is quite unprincipled and cannot even be said to rob the rich to pay the poor. Barlowe observes that in many American cities the typical landlord is an elderly or retired individual whose rent constitutes a major part of his livelihood and whose average net income is frequently less than

that of his tenants (9). Similarly, a survey in Britain suggests that investors in rent-controlled houses seldom have much capital and are typically elderly (10). In South Africa the right to occupy rent-controlled housing is not linked with any means test and there are some apartment blocks of high quality in which well-to-do tenants enjoy rents markedly below those which would prevail if market forces were permitted to operate. Backman (11) states that in New York in 1947 the purchasing power of rent was only 63.4 per cent of what it had been in 1939 (when business conditions were poor and there was a high vacancy rate). It is probable that by 1950 the real income of property owners had fallen to about two-fifths of its 1939 level. During this period a marked expansion in income had characterized the American economy, but not only had landlords failed to share in this, there had actually been a sharp decline in their real income. In an article by Denman (12) it is recorded that in Britain between 1938-9 and 1958-9 wages and salaries rose by 343 per cent, but rent showed a rise of only 48 per cent. Thus while the risks of property investment remain with landlords the appreciation in value is transferred to tenants.

DETERIORATION OF PROPERTY

With rent control the income of landlords ceases to be related to the state of repair of the building so that they become both less

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- (9) "Land Resource Economics", page 182.
- (10) See Thorncroft, "Principles of Estate Management", page 274. See also Needleman, op. cit. page 163, and Pennance and Gray, op. cit. page 1.
- (11) "Impact of Rent Control upon Income", Appraisal Journal 1951 page 17. Regrettably, there is a dearth of statistical information in South Africa showing the effect of rent control, but there is no reason to consider that experience revealed by statistics from abroad is dissimilar to what has happened in South Africa.
- (12) "Realism about Rents", The Times, 6th and 7th September, 1960.

willing and less able to maintain buildings. In America in the period 1939-49 there was a much larger rise in the expenditure on owner-occupied buildings than on tenant-occupied buildings (13), and in New York the expenditure on maintenance and repairs in 1947 was actually 3.4 per cent lower than in 1939 (not allowing for the considerable inflation which had taken place between those two years) (14). Macrae observes that in Britain rent control has caused nearly six million houses to deteriorate rapidly towards slum conditions as a consequence of their rents being frozen between the 1930s and the mid-1950s, a period in which repair costs trebled (15). The cost of maintaining a house in good repair rose in Britain by over 200 per cent between 1939 and 1953, but the rent of many controlled tenancies did not change. The cost of routine maintenance sometimes exceeded the controlled rent (16). In France it is uneconomical for landlords to keep property in repair and the problem of slums is causing concern (17). Whilst no relevant statistical data appears to be available in South Africa, there can be no doubt that rent control has been a major factor in the creation of slums. It is to be noted that the presence of rent-controlled buildings in a neighbourhood will be a major factor in the onset of blight and will discourage redevelopment of adjoining properties. There is an interesting link between the State's interference with the price mechanism in imposing rent control and its subsequent action in attempting to remedy the defects in the operation of the price mechanism through urban renewal. It is to be wondered how often the need for urban renewal would not have arisen if rent control had not been imposed.

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 (13) Backman, op. cit., page 12.

(14) Backman, op. cit. page 15. For analysis of the effect of rent control on property in New York, see Grebler, "Experience in Urban Real Estate Investment".

(15) Op. cit., page 21.

(16) Needleman op. cit. page 164.

(17) Roselli, "Residential Property - France", Estates Gazette, 11th January, 1964, page 99.

DECREASE IN RENTED ACCOMMODATION

Where rent control is imposed, the sum of the tenant's right to remain in occupation (which is not marketable as it cannot be transferred) and the landlord's right to receive the controlled rent is less than the price which would be paid by a purchaser who intended to occupy the property himself (18). So, if the landlord is able to sell the property to a prospective occupier, he will do so because he will obtain a higher price than an investor would pay. Thus owner-occupiers bid rent-controlled property away from owner-investors (this argument is obviously less applicable to buildings with more than one occupant). The freedom of choice of occupiers is limited and they are forced to buy rather than hire accommodation and may be compelled to make capital investments (and to incur indebtedness) which they can ill afford. In America between 1940 and 1950 the number of non-farm single-family detached units increased from 16.4 to 23.0 million while the number of tenant-occupied units decreased from 6.2 to 5.3 million (19). In the period 1939-49 the rent of tenant-occupied non-farm dwellings rose by 36 per cent while the rent imputed to owner-occupied non-farm dwellings rose by 140 per cent, reflecting the rise in the costs of labour and materials (20). Similarly, in Britain in 1945 houses with vacant possession (i.e. those purchased by prospective owner-occupiers) sold at an average price of 80 per cent above the 1934-9 level, but those without vacant possession (i.e. those which had to continue to be held as investments) at only 30 per cent in excess of the previous level (21). Between 1947 and 1961 privately let unfurnished accommodation fell

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(18) See Turvey, *op. cit.*, pages 21-2.

(19) Barlowe, *op. cit.*, page 180.

(20) Backman, *op. cit.*, page 12.

(21) Turvey, *op. cit.*, page 45.

as a proportion of all accommodation from about half to just over quarter (22). By December, 1967, it had fallen to 17.9 per cent (23).

In these circumstances it was obviously not a proposition for the owner of a rent-controlled property to continue to hold it as an investment when he could sell it to a prospective occupier.

CONTROL DETERS DEVELOPMENT

Because it ceases to be economic for investors to own rent-controlled property, the development of accommodation to let is deterred. To some extent the non-availability of accommodation to hire will increase the demand for the development of accommodation for owner-occupation, but the overall effect of rent control will be to cause a decline in the total volume of development. For the development process to be thus impeded it is not necessary for new accommodation to become subject to control on completion; it is sufficient that there should be a political threat of control in the future (24). In Britain it has become uneconomic for private enterprise to build residential accommodation for letting and consequently three-quarters of the privately-held housing let is over 75 years old (25). The stock of privately-held dwellings is in fact being reduced at a rate of at least 3 per cent per annum (26).

In France rent control has also caused residential construction to

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(22) Needleman op. cit. page 124.

(23) See Estates Gazette 9th November, 1968, page 615.

(24) Rent control also frequently retards development by giving the tenant a statutory right of occupation.

(25) Macrae, op. cit. page 24.

(26) Needleman, op. cit. at page 185.

be limited to high-cost rental units (27) and owner-occupied units, and there is a serious shortage of accommodation. In Paris in 1948 only 11 per cent of the residential buildings in the city had been erected after 1914 and less than 1 per cent since 1936 (28). It is apparent that rent control, far from stimulating the development of modern housing, encourages the continued use of inferior accommodation through providing its occupants with subsidies and in consequence of the threatened imposition of control on new development.

ARBITRARY REDIRECTION OF EXPENDITURE
TO OTHER SECTORS OF THE ECONOMY

Rent control diverts consumer expenditure from housing to other goods and services. It also turns investment from property to other avenues and consequently decreases the demand upon the building industry. But it does not curb inflation because, in the absence of general price control, its effect is merely to redirect expenditure from rent to other consumer items. This distortion in the pattern of demand to the detriment of landlords and in favour of investors in other sectors of the economy is illustrated by American experience. Between 1939 and 1950 wages, construction costs and the cost of food rose by more than 100 per cent, but the index of rentals only increased by 30 per cent (29). In the period 1939 to 1949 the rise in the rent of tenant-occupied non-farm buildings was only about one-fifth of the total increase in consumption expenditure. A serious consequence of prolonged rent control is that tenants become unaccustomed to paying economic rents; they begin to think that controlled rents are normal and that they have a right to subsidized accommodation. The longer rent control persists the more

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(27) Paradoxically the effect of imposing rent control on low-cost units but not high-cost is to encourage the development of the latter at the expense of the former.

(28) Barlowe, op. cit., pages 181-2; Roselli, loc. cit.

(29) Barlowe, op. cit. page 179.

politically difficult does its removal become.

DISRUPTS ALLOCATION OF SPACE

Where rent control is imposed, the price mechanism ceases to function as the allocator of accommodation, with the consequence that its distribution is dependent upon past events rather than present needs. The older generation is subsidised at the expense of the younger. Macrae observes that in the period 1945 to 1955 in Britain it was the children of young families forced to live in overcrowded conditions during their formative years who were most hurt (30). Not only does rent control lead people to occupy space in excess of their needs in order not to forgo a subsidy (31), but for the same reason it also discourages the retired from moving away from their former places of work, with the consequence that employed persons either have to commute or to live near their work place in overcrowded conditions (32).

DETERMINATION OF RENT

We now turn to the question of the amount at which the controlled rent is fixed. In South Africa in terms of the Rents Act, 1950 (33), as amended, rent is fixed at a percentage of 'value'. The provisions of the Rents Act relating to the determination of rent and the interpretation that the courts and legal commentators have placed upon

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(30) Op. cit., page 18.

(31) The most common size of house for people living alone in Britain in 1951 consisted of 4 rooms. See Needleman op. cit. page 184. In a recent survey of 200,000 dwellings subsidised by the Greater London Council it was found that 60,000 had one spare bedroom, of these 30,000 had two spare bedrooms and 6,000 three spare bedrooms. See Estates Gazette 23rd November, 1968, page 882.

(32) See Macrae, loc. cit., generally on the effect of rent control on the allocation of accommodation.

(33) Act No. 43 of 1950.

the word "value" can only be attributed to absence of an understanding of economic principles. Bonbright (34) has made the following comment:

"The striking nature of this rift of thinking between persons trained in economics and persons trained in law was impressed upon the writer ... when he offered simultaneous courses on valuation and (public) utility economics in the Columbia University Law School and in the Harvard University Department of Economics. When the law students were presented with the assertion of the economist that "value" is a logically unsound basis of (public utility) rate control, many of them at once took issue and remained unconvinced at the end of the session. But when the same viewpoint was presented to the economics students, they accepted it as a truism too obvious to warrant discussion."

The problem involved in the fixing of public utility rates (e.g. the charge for electricity) is similar to that in the case of rent control, and the remarks of Bonbright have equal application to the latter. In South Africa the return allowed of 6 per cent on land and 8 per cent on buildings (35) in terms of the Act is of little comfort to property owners, because the valuations on which the returns are based are arbitrary. The valuation of an investment can only be made by capitalizing predicted income, but this procedure cannot be applied because the Act renders income unpredictable. The provisions of the Act are thus in conflict with the basic economic principles of valuation. Although reference is made to 'reasonable rent value' (36), there is no objective test of reasonableness. Indeed, it is specifically provided that the rent need not coincide with market value (37). The application of the Act to property which is at present controlled has in practice resulted in

.....
(34) "Valuation of Property", Volume II, page 1082.

(35) Rents Act, sec. 1 (ix) (a), (b).

(36) Sec. 1 (xiii).

(37) Sec. 1 (xiii).

rent levels greatly below those which would prevail if control were lifted. The justification for this is not apparent to the writer. All residential property (subject to certain exceptions) that was occupied before 21st October, 1949, is automatically controlled and all residential property of more recent date and all business premises can be controlled at the pleasure of the Minister (38).

'Reasonable rent' as provided for by the Act is in effect such rent as a rent board considers to be reasonable, and there is in practice no limit upon its discretion (39). Although the discretion of the rent board should supposedly be exercised judicially and not capriciously, it is in fact inevitable that its decisions will be arbitrary because the legislation destroys the price mechanism and with it any basis for the determination of rental value.

In assessing 'value' a rent board is entitled to take account of the 'actual cost' of erecting buildings, municipal valuations, sworn valuations and building society valuations (40). The building cost referred to is presumably the original cost and not the present cost

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- (38) Secs. 33. The automatic control of business premises first occupied before 21st October, 1949, is in suspense. See R.E.G. Rosenow and M.A. Diemont, "The Rents Act in South Africa", 3rd ed. (1965), page 17.
- (39) See *Durban Rent Board v. Edgemount Investments Ltd.*, 1946 A.D. 962, esp. at 974; *G.A. Flats (Pty.) Ltd. v. Pretoria (Eastern Areas) Rent Board*, 1949 (3) S.A. 1100 (T) at 1102. Colman J., in the case of *Lukral Investments v. Rent Control Board*, Pretoria, 1969 (1) S.A.496 (T), takes a somewhat more restrictive view of the discretion of the Rent Board, stating that he "cannot impute to the Legislature the intention to legislate in so disingenuous a fashion" (page 504). Doing the best that he could "with this inadequate material" he formed the view that "rentals of buildings in which there is comparable letting accommodation will ... be properly taken into account, together with other data, in the pursuit of the elusive value which is not current market value."
- (40) Sec. 1 (xiii).

of replacement and (in the light of the depreciation of the building since erection, of its appropriateness as an improvement of the site or of inflation which has taken place since it has been built) may be quite unrelated to its present value. The object of taking into account rating assessments which are not necessarily designed to establish value, building society valuations which are intentionally conservative, and sworn valuations which may or may not be correct, is not clear. The purpose of the exercise ought correctly to be an analysis of the factors which produce value.

It emerges from the judgments in *Durban Rent Board v. Edgemount Investments, Ltd.* (41) that the factors which a rent board is directed to consider in determining value suggest an intrinsic value of a more enduring nature than one dependent on temporary market fluctuations (42). The fallacy of such a concept will be readily apparent to any person with a smattering of economics. Value is a function of supply and demand at any moment in time and a pound of diamonds has no more intrinsic value than a pound of mealies. The greater current value of a pound of diamonds is attributable to the relative scarcity at the present time of diamonds in relation to the demand for diamonds as compared with the supply of mealies in relation to the demand therefor. Similarly, the value of property is entirely dependent upon current demand and supply conditions (43).

The Edgemount decision laid down that a rent board ought first to determine a 'reasonable' quid pro quo for the accommodation, leaving capital value out of consideration, and thereafter 'value' should be employed as a test to determine whether the rent was a proper percentage of 'value' (44). It has only to be considered that the value of any asset is to be found by discounting the anticipated

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(41) 1946 A.D.962 at page 973.

(42) Rosenow and Diemont, op. cit. page 71.

(43) See Chapter IV page 82 above.

(44) See Rosenow and Diemont, page 73.

future benefits flowing from its ownership and that value is therefore a function of rent, for the impracticability of this procedure to be apparent.

Rosenow and Diemont write (45):

"The determination of 'value' remains a difficult proposition. It must remain irregular to calculate backwards from the rent determination, because there would in that event be no appropriate test.

It must be emphasized that the legislature could scarcely intend that the 'value' of the property can be altered so as to suit the rent determination. Theoretically the rent board is supposed to operate in terms of a certain percentage and this percentage does not exist, if it can be pushed up or down at the will of the board. A bona fide determination of 'value' as apart from the previous assessment of rent, must therefore be made.

It is suggested that the best method to adopt will be to determine 'market value' in the first instance, taking into consideration whether or not the cost of erection, the municipal valuation, or the sworn appraisement, could be said to approximate to such value, and bearing in mind also the purpose for which the property is being used.....

Having arrived at the market value of the property, the next problem before the board is whether the value is ... a reasonable rent value. ...

After arriving at a proper rent value the rent previously determined should be tested, but there should be no juggling with the valuation, so as to make it fit the rent."

It seems to the present writer that commendable though such an attempt to induce meaning into legislation may in itself be, it is without avail in the present case. It is better to state that the wording

.....
(45) Op. cit., pages 73-5.

of the Act is quite meaningless, that it is incapable of rational interpretation and that such intellectual garbage should be replaced with something intelligible if the legislature wishes to impose rent control.

The Act provides that the value of land and buildings must be assessed separately. It is recognized that buildings have no independent value and that the figure for the buildings has to be found by deducting the value of the land from the value of the property as a whole (46). The impossibility of finding the value of the whole in terms of the Act has already been discussed. However, the market value of the site (47) can be found by the normal process of comparison with actual sales, but it would have to be borne in mind that site value is residual (being the difference between the capitalized predicted income of an economically optimum development and the building cost of such a development) and that, even where only part of the stock of residential accommodation is controlled, rent control will have repercussions throughout the market because of its impact upon the operation of the price mechanism. If, as Rosenow and Diemont suggest, the rent has first to be determined and an independent determination then made of value, it is to be wondered how rent is to be allocated as between site and building - a necessary procedure as the Act provides that the return on the land should be 6 per cent and the return on buildings 8 per cent (48). The writer can see no justification for the rule apparently adopted by rent boards that the value of land should not exceed one-third of the value of the building (49): there is no necessary relationship between the value of a site and the value of a building. The

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(46) Sec. 1 (xiii), provisos (i) and (ii).

(47) Note that for purposes of the Act the 'value' of the site will not necessarily equal its market value. See sec. 1 (xiii).

(48) Sec. 1 (ix) (a), (b).

(49) Rosenow and Diemont, op. cit., page 75.

provision of an identical percentage return for all properties is also unsound because the risk, liquidity and ease of administration of different properties will vary vastly, as is evident from the range of yields in the market place. It is also obvious that for the average residential investment the percentages allowed are too low. It is of interest that depreciation is allowed as an expense by the Rents Act (50) but not by the Income Tax Act (51) (subject to certain exceptions in respect of factories and hotels) and arguable that for purposes of the Rents Act the figure should be grossed up in order to allow for the fact that it will have to be provided for out of taxed income.

A more reasonable basis for control in those abnormal and temporary circumstances where control may be justified is to tie rents to a cost-of-living index, as is the case in Sweden (52). An alternative might be to limit the permissible increase in any year to a fixed percentage of the rent for the previous year.

A NOTE ON BUILDING CONTROL

In a free enterprise economy the price mechanism allocates the amount of capital devoted to building and establishes an order of priority between the claims of competing forms of building construction. In this way the nearest possible approximation to the community's preferences in respect of land development is achieved. In extreme circumstances it may become necessary for economic planning temporarily to suspend the workings of the price mechanism. Nevertheless once the test of the price mechanism is abandoned it becomes extraordinarily difficult to judge how the resources of the building industry should be allocated between competing uses,

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(50) Sec. 1 (ix) (g).

(51) Act No. 58 of 1962. See secs. 11 (e) (ii) and 13.

(52) Barlowe, op. cit. page 182.

particularly in view of the dearth of statistical information in the Republic. For example, the merits of the claims of an air-conditioned office building as against a house or a factory are not as obvious as superficial observation might indicate - an expanding economy requires a continuing supply of efficient offices. Nor is inflation a sound reason for building control because anything less than total control of all facets of the economy only leads to redirection of expenditure and distortion in the pattern of demand. Controls are a tool to remedy temporary deficiencies in the working of the price mechanism and not an end in themselves.

CHAPTER IX

CONCLUSION

To an important extent, where unsatisfactory approaches to problems have been revealed in this study, they have been attributable to a failure on the part of legislature or judiciary to understand the valuation process. Typically it has not been appreciated that value is the point of equilibrium between supply and demand, that the thing to be valued is the anticipated future benefits flowing from a property, that these anticipated benefits have to be discounted to find the present value, and that there is no rational basis for finding value through deducting depreciation from replacement cost. The second chapter dealt at some length with the concept of value and with various methods by which allowance could be made for the fundamental element of time in differing circumstances. Specifically and by implication these procedures have been employed in considering the subject matter of chapters III to VIII. It is believed many pitfalls could have been avoided had essential valuation principles been grasped. In this concluding chapter certain proposals will be put forward which it is suggested would provide a better approach to the problems arising in land usage in South Africa.

A TRAINED PROFESSION

The question arises whether property economics is merely an amalgam of elements from other disciplines or a distinct branch of learning with a central core of its own peculiar material. It is submitted that the unique contribution of the property economist centres upon the economic assessment and valuation of property. While he requires

a knowledge of applied economics in the fields of land and development, of several branches of law, of town planning and of finance, his work is more than the mere aggregation of these skills. In the words of the hand-book of the Land Economics Tripos at Cambridge University "the use and ownership of land is a combination of economic, legal and technical factors and it is the inter-relationship of these contributory factors that provides the substance, uniqueness and coherency of land economy as an independent subject".

At the outset of chapter III it was stated that the function of the economist in town planning was to identify anticipated costs and benefits arising from planning proposals in order that resources should be rationally allocated. Similarly, in the private sector he will have to weigh the economic consequences of the alternative courses of action which are presented in any set of circumstances. Property economics, to which this thesis is intended to be a contribution, is micro- rather than macro-economics. The property economist needs to be equipped with a detailed and specialist knowledge of certain aspects of urban economics; he also requires an extensive knowledge of law because of the legal complexity of the commodity with which he deals. His work in both the public and the private sectors bridges a gap between other disciplines in a field which is becoming increasingly inter-disciplinary. He knows less about town planning than the planner, less about urban geography than the geographer, less about discounting techniques than the actuary and less about sociology than the sociologist, but he possesses a sufficient knowledge of these and other relevant activities to perceive their inter-connection and to be able to comment upon the economic consequences of alternative proposals for the employment of resources.

From the contents of this thesis it will be apparent that the property economist should know how his skills relate to a total problem, but he will not necessarily be concerned with the total. While he will play an essential role in town planning, he will recognise that there

can be overriding considerations which fall outside the scope of his contribution. In expropriation he will not have to justify the purpose for which land is taken, but will seek to establish the most accurate figure of compensation (on whatever test may be applied). Similarly, in rating he will be concerned with the basis of assessment rather than the overall policy of taxation, although he will be ready to point out the effects a particular system is likely to have on the real estate market. In rent control, likewise, he will wish to minimise distortion in the operation of the price mechanism, but primarily he will be concerned with the establishment and implementation of satisfactory methods of controlling rent.

A degree in property economics was commenced at London University in 1918 and at Cambridge in the following year. Although teaching and research in land economics began in the United States at the University of Wisconsin in the 1880s, it was not until around 1919 that it was organised as a special focus of interest. In the 1920s the number of academic institutions providing formal courses multiplied very rapidly. By 1960 there were some 60 colleges and universities in the United States which offered a sequence of courses in real estate as a curriculum leading to a Bachelor's degree. Unlike the British universities, property economics in the United States is usually taught within the business school and not in a separate specialised faculty (1). Because the practice of property economics is intellectual, varied and discretionary to a high degree it is essentially a university subject and a proficient body of practitioners cannot be expected to emerge from the introduction of examinations by the Institute of Estate Agents or the Institute of Valuers or by any

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- (1) See Dean "Developments in Estate Management at Cambridge University" R.I.C.S. Journal, August 1949; Denman "The Core of Professional Knowledge", Chartered Surveyor, September 1961; Fischer "What should be included in a Real Estate Examination?", Appraisal Journal, July 1954; Lichfield "United States Real Estate", Estates Gazette, November 18, 1967.

other similar body (2). Nothing would be accomplished by repeating the pattern which exists in Britain where there are several competing bodies claiming to be professional societies but (with one recent exception) conducting examinations with lower entrance standards than those required for university degrees (3). Nor are the technical colleges appropriate places for the development of property economics as an academic discipline. An encouraging development in South Africa has been the establishment (at the Universities of the Witwatersrand and Cape Town) of degrees in town planning which include courses in urban economics with some examination of land economics. It is to be hoped that the Business Schools which are being established at our universities will also introduce land economics courses and that ultimately it will develop as an identified field of specialisation.

A SPECIALIST TRIBUNAL

An understanding of valuation is not acquired without prolonged study and experience. Mention has already been made in chapters VI and VII of the necessity for a specialist tribunal to hear valuation cases. It is hardly possible for a court, untrained in valuation matters, to obtain a true understanding of a complicated valuation problem during the trial of one issue. The writer is not alone amongst those who have been expert witnesses in valuation cases in thinking that the real issues are often obscured by the mass of evidence led by counsel who themselves may have difficulty in appreciating the problems involved or in following the application

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- (2) It should not be thought that these societies do not perform an important role. In the field of real estate different functions have to be conducted calling for differing ranges and levels of skills. The point is simply that the task of the property economist is at another level.
- (3) The trend in Britain today is for an increasing percentage of those intending making a career in property to obtain a degree qualification in property economics.

of valuation techniques. The only answer to this problem is the establishment of a specialist tribunal. In Britain there is a now well-tried and admirable model which it is suggested should be broadly copied in South Africa - the Lands Tribunal. This body was constituted in 1949 and is presided over by a President who must be a judicial officer or a barrister of at least seven years' standing. The number of other members of the Tribunal is within the discretion of the Lord Chancellor; they must be either barristers or solicitors, or persons with experience in real estate valuation. In practice apart from the President there have usually been four or five other members drawn equally from the legal and valuation professions. Appeals from the Tribunal lie to the Court of Appeal and consequently the Tribunal has much of the respect traditionally accorded to the High Court. The Tribunal hears expropriation cases and compensation cases arising under planning legislation. It acts as a court of appeal from Rating Valuation Courts and from the Commissioners of Inland Revenue. In addition it conducts a number of similar functions such as the hearing of applications for the discharge or modification of servitudes.

The jurisdiction of the Tribunal may be exercised by any one or more of its members, the President selecting a member or members to deal with a particular case or class of case. Where an issue is likely to raise special difficulties normally both legal and valuation members will be represented. The decisions of the Tribunal must be written and reasoned. Its decisions are final except in matters of law from which an appeal lies. Where a question of law is in dispute the Tribunal is required to state its decision and the alternative valuation which it would have awarded had it decided otherwise on the question of law. The remedy of an aggrieved party is to require the Tribunal to state a case for the decision of the Court of Appeal, and in the event of the appeal being upheld the Tribunal will accordingly make an amendment to its decision. Whilst the Lands Tribunal is not in any way bound by precedent, the publication of decisions has been successful in providing guidance for the

future and comparatively few cases have been stated for opinion by the Court of Appeal (4).

There seems to the writer to be every reason for following the example of the Lands Tribunal in South Africa and constituting a similar body by Act of Parliament to hear expropriation, rating, rent control and all other matters involving real estate valuation, either as a tribunal of first instance or on appeal from other bodies. In consequence of the large geographic area of the Republic it might prove desirable for the tribunal to have provincial divisions, but it may be that this would not be justified by the volume of cases to be tried and that costs and the necessity for uniformity of decisions would dictate that there should be one central body which could be peripatetic. An essential requisite is that the membership of the tribunal should be for a period of years. The decision of the tribunal should be final except in matters of law, in respect of which there should be an appeal to the Appellate Division. The tribunal would thus have similar status to a division of the Supreme Court.

THE ALLOCATION OF LAND RESOURCES:

THE MARKET OR THE STATE?

It is possible for all the land resources of a society to be allocated by state decision and there are examples of economies, such as the Russian, in which this is the case; the contrary extreme, a wholly market allocation of real estate resources, is not exemplified because for reasons explained in chapter III it cannot exist. The difficulty of creating markets for certain commodities and services, the scale of investment and sometimes length of time before a return on investment can be obtained, and the prevalence of monopoly because

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- (4) For a discussion of the Lands Tribunal in Britain see Yardley: "A Sourcebook of English Administrative Law"; Garner: "Administrative Law"; and Lawrance and Chavasse: "Compulsory Purchase and Compensation", 2nd Edition.

of the fixity of location make it impractical for allocation to be wholly through the price mechanism operating in a free market. From the time of the Industrial Revolution, with the development of railways (which even if privately owned required the assistance of the State to expropriate land), the participation of the State has become increasingly necessary. To what extent allocation should be the function of the State and to what extent it should fall to private enterprise is a matter of political debate beyond the scope of this study. Moreover, there is ultimately no objective test that can be applied; such criteria as exist are not merely economic but also sociological and, as is clearly demonstrated in South Africa, more broadly political. It is the belief of the writer that because of the weakness of planning tools (5) the market is the more efficient allocator in purely economic terms and should be utilised wherever it is feasible for it to operate and there are not overriding reasons of state policy demanding central action (6). In those circumstances where state intervention in the operation of the market is considered necessary or desirable, the minimum distortion should be created and the least modification of "value" should occur (7). The concepts of "value" and "valuation" (8) should be

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 (5) See discussion in Chapter III, pages 63-67, above.

(6) There appears to be some disillusionment today amongst town planners with the potentialities of central decision making. See passage quoted from West above Chapter III page 67. Professor E.W.N. Mallows in a paper to be published shortly writes: "We no longer want to remodel our towns as one person operating according to reason: the problem seems to us far too complex. We are now moving rapidly into anti-Cartesian territory and ... it is important to emphasise how urban theory is leaving the over-simple concepts of formal order derived originally from a Cartesian approach to an urban problem never fully stated".

(7) This view is to be contrasted with that of Ratcliff on the one hand, and Lean and Goodall on the other. See above Chapter III pages 40-43.

(8) See above Chapter II page 6.

distinguished, and where a figure of value has to be found legislation should be so couched that the principles of valuation are observed and the resultant figure accords with market value (9).

.....

(9) Except in circumstances where equity demands that the figure to be found is "value to the owner". See above Chapter II page 11 and Chapter IV page 70.

APPENDIX A

RECAPITULATION

It is the purpose of this concluding appendix to reiterate and thus emphasise what seem to the writer to be the more urgent and important conclusions arising from this study. The subject matter is dealt with seriatim rather than in any necessary order of significance.

CHAPTER 2

Although the valuation process is subjective to the extent that the data employed are imprecise, its methods are essentially scientific. The forecasts and calculations of the appraiser should be included in the valuation report and the degree of uncertainty thought to attach to any prediction should be stated. The replacement cost approach should be used as a last resort and only in circumstances where there are no data available upon which to base the methods of direct or indirect comparison. The method of indirect comparison is normally to be employed in the valuation of investment, commercial and industrial property.

CHAPTER 3

Economics ought to be regarded as an integral and utterly vital part of the town planning process and not as an antipathetic device. The principal objective of town planning should be seen to be the improvement of the market's efficiency in the allocation of land resources in order to maximise economic welfare. The basic

function of urban renewal is to prime the pump of private enterprise in the elimination of blight (as defined by Davis and Whinston) and not the removal of slums or the implementation of racial policy. The powers taken by the Central Government in South Africa to disregard the town planning schemes of local planning authorities and to freeze private development should be abandoned. Town planning should be seen to be an essentially local and not central government function, the market should be the predominant allocator of land resources, and the execution of urban renewal schemes should be principally through private enterprise. Cost-benefit analysis should be applied to all major town planning decisions, but its limitations should be realised and it should not be used to cloak planning decisions with the trappings of scientific objectivity.

CHAPTER 4

The administrative method of expropriation procedure presently employed in South Africa is weighted heavily against the private citizen and should be replaced with the judicial decree method. Compensation should be the higher of market value or the value to the owner, provided that where legislation lays down that compensation is to be at "market value" courts should interpret this term liberally in order that the person whose property is taken should be financially as well off after such taking as before. South African legislation should be amended in order that compensation may be paid to all persons with rights in property, not merely to those holding registered rights. Provision for the assessment of severance damage by the "before and after" method should be inserted in the Expropriation Act, 1965. Similarly a material detriment clause should be included in the Act. The expropriation provisions of the Cape Municipal Ordinance 1951 should be jettisoned. The provisions of the Community Development Act 1966 relating to valuation are thoroughly unsatisfactory and require radical amendment.

CHAPTER 5

Compensation ought always to be paid when a zoning regulation is promulgated which adversely affects the value of property and which does not constitute a reasonable exercise of the police power of the State. It follows then that when the value of property is reduced by the amendment of zoning provisions relating to it in terms of an established scheme, compensation must always be paid because it cannot be held that the provisions of the scheme in force are so contrary to "general welfare" as to merit the exercise of the State's police power. On the other hand, if land is rezoned to permit a higher use and there is a fall in the value of other land consequent upon the increase of the total supply of land zoned for the particular purpose, this circumstance is part of the normal hazard of property ownership and no compensation should be paid. It must be accepted either that changes in the value of land (in the absence of specific State interference) are part of the risk assumed by the purchaser of land, or that the State should bear the hazard and not only charge landowners who enjoy increases in land value but subsidise those whose land is reduced in value. The more realistic approach is that the State has no obligation to indemnify where land falls in value other than through an act committed by the State itself, and that similarly the State has no right to betterment. Any proposed zoning amendment should be judged on its planning merits and not influenced by some charge it might be possible to impose on the landowner. In the Cape and Natal the keeping of town planning schemes in an interim stage to avoid the payment of compensation if the scheme is amended adversely to the interests of an owner is to be condemned. The betterment provision in the Transvaal Ordinance No. 25 of 1965 is based upon unsound assumptions and ought to be repealed. Similarly, the endowment provisions existing in the Ordinances of all four provinces are unsatisfactory.

CHAPTER 6

Rating as a system of taxation should only be employed in circumstances

where the expenditure of rates is beneficial for property owners or occupants as a whole. Revenue for other local purposes should be raised by other means for there is otherwise no justification for singling out real estate as a basis for taxation. For purposes of rating all property should be assessed at market value in existing use and not market value in potential use, nor at value to the owner; arbitrary methods of assessment such as the summation procedure should not be employed. The flat system of rating should be employed exclusively. It follows that substantial changes in existing rating practices in South Africa should be made because throughout the country rates are employed to finance expenditure which is not beneficial to the occupants of property and are levied on potential use; in important sections of the country the flat system of rating is not implemented and in many towns site rating only applies. The replacement cost approach to valuation which is used in Natal, the Cape and the Orange Free State should be abandoned. The Cape Valuation Ordinance No. 26 of 1944 is essentially absurd and requires radical amendment. There is urgent need for reform of the practice in the Transvaal, the Orange Free State and Natal whereby assessments for rating purposes are conducted by the local authorities. As few judges or arbitrators can possess any knowledge of land economics it is desirable to establish a specialist division of the Supreme Court to hear rating and other cases where the problem of real estate valuation arises. Legislation is required to compel administrative and quasi-judicial bodies which decide real estate valuation disputes to state the reasons for their findings.

CHAPTER 7

In the valuation of township land or land with township potential an actuarial analysis should be employed in all circumstances where there is evidence upon which to base the method of direct comparison. The "thing" to be valued is the effective economic interest in the hands of the owner, and the method of registration in the Deeds Registry is not relevant.

CHAPTER 8

Rent control is tantamount to taking property without compensation and, for this reason and in consequence of its other deleterious effects, should only be resorted to in circumstances of extreme emergency, such as war, which necessitate the suspension of the normal operation of market forces. Apart from its injustice to the owners of controlled property, the effects of rent control are the deterioration of buildings, the decrease in rented accommodation to which it leads, its deterrent effect upon development, its arbitrary redirection of expenditure to other sectors of the economy, and its disruption of the allocation of space. The provisions in the Rent Act 1950, as amended, for the determination of controlled rental are quite meaningless and either they should be amended forthwith or the Appellate Division should seize upon its first opportunity to state that they are unenforceable.